SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1933

No. 114

THE STATE CORPORATION COMMISSION FOR THE STATE OF KANSAS, HOMER HOCH, JESSE W. GREENLEAF, ET AL., APPELLANTS,

vs.

THE WICHITA GAS COMPANY, THE HUTCHINSON GAS COMPANY, THE NEWTON GAS COMPANY, ET AL.

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE DISTRICT OF KANSAS

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[fol. 5]

IN UNITED STATES DISTRICT COURT FOR THE DISTRICT OF KANSAS, FIRST DIVISION

In Equity. No. 1637-N

THE WICHITA GAS COMPANY, a Corporation, Plaintiff,

vs.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS and Jesse W. Greenleaf, Thurman Hill, and C. W. Campbell, as Members of said Commission, and Roland Boynton, Attorney General of the State of Kansas, Defendants

Bill of Complaint—Filed Sept. 19, 1933

Comes now the Wichita Gas Company, a corporation, and alleges:

1

That it is a corporation duly organized and existing under the laws of the State of Kansas, with its principal office, place of business and post office address at Wichita, in said state.

[fol. 6] 2

That the Public Service Commission of the State of Kansas is a legislative and administrative body created by the laws of the State of Kansas, having its office and principal place of business in the City of Topeka, Kansas, and is within the jurisdiction of this court. The defendants, Jesse W. Greenleaf, Thurman Hill and C. W. Campbell, at all times complained of herein have assumed to act as members of said Commission; that Roland Boynton is the duly elected and acting attorney general of the State of Kansas.

3

That the plaintiff is a resident and citizen of the State of Kansas and each and all of the defendants are residents

and citizens of the State of Kansas. The amount in controversy herein is more than $3,000.00 exclusive of interest and costs.

4

That this is a suit in equity arising under and involving the construction and application of the Constitution and Laws of the United States in that plaintiff is herein seeking to have permanently enjoined certain orders of the Public Service Commission of the State of Kansas, issued August 31st, 1932, for the reason that the same are unconstitutional, null and void because repugnant to the Fourteenth Amendment to the Constitution of the United States and the First Sub-Division of Section 10 of Article 1 of the Constitution of he United States, Clause 3, Section 8, Article 1 of the Constitution of the United States, in that said orders deprive plaintiff of its property without due process of law, [fol. 7] deny it the equal protection of the law, impair the obligation of its contracts, undertake to legislate with respect to interstate commerce and usurp the business management of plaintiff company.

5

That plaintiff is engaged in the business of distributing and selling natural gas for all purposes in Wichita, Kansas, and vicinity and is a public utility under the jurisdiction of said defendant Commission.

6

That plaintiff does not produce or manufacture gas and has no supply for sale and distribution to its customers other than the supply it purchases from the Cities Service Gas Company at the agreed price of forty (40) cents per thousand cubic feet for domestic purposes; that said Cities Service Gas Company refuses to sell domestic gas to plaintiff for a less price and plaintiff has no other source of supply available to it, and without its present supply cannot carry on its said business.

7

That the present value of plaintiff's property used and useful in rendering the service in which it is engaged is not less than the sum of $2,872,854.00; that it is operating under

the jurisdiction of said Commission and is charging for all gas sold by it for domestic purposes rates heretofore es-
[fol. 8] tablished and approved by said Commission; that under said existing rates its net earnings for the year ending June 30th, 1932, were $181,096.00, which constitutes an earning of only 6.3 per cent on the present fair value of its property for return and depreciation and which earning is unreasonably inadequate and confiscatory.

8

That notwithstanding the experience of plaintiff under existing rates and the inadequacy and unreasonableness of its present earnings, said defendant Commission under date of July 2nd, 1931, on its own motion issued an order in its docket number 13127 entitled, "In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company," by the terms of which it ordered this plaintiff and nine other corporations engaged in the sale and distribution of natural gas in approximately one hundred cities and communities in the State of Kansas to appear and furnish to the Commission such evidence as they might desire or the Commission might require as to the reasonableness of certain contracts. A full, true and correct copy of said order is hereto attached, marked Exhibit "A," and made a part hereof.

9

That pursuant to said order, Exhibit "A," plaintiff appeared specially before said Commission and objecting to the jurisdiction of the Commission; filed its special appearance, a full, true and correct copy of which is hereto attached, marked Exhibit "B," and made a part hereof.

[fol. 9] 10

That from the date of the issuance of said order, Exhibit "A," up to and including February 16th, 1932, numerous hearings were had before said Commission in which evidence was introduced by this plaintiff, by the other respondents to said proceeding, and by expert witnesses, engineers and accountants employed for the special purpose by said Commission itself.

11

That on July 20th, 1932, said Commission handed down its opinion, findings and order in said proceeding, a full, true and correct copy of which is filed herewith, marked Exhibit "C," and made a part hereof, the same being too voluminous to attach hereto.

12

That by said opinion, findings and order said Commission undertook to find unreasonable the contract between plaintiff and Henry L. Doherty & Company and undertook to order plaintiff to discontinue the setting up on its books of any payments due or to become due thereunder and to dicontinue making any such payments; undertook to find that the contract between plaintiff and the Cities Service Gas Company, under which it purchases its entire supply of gas for distribution in its said business, was unreasonable and undertook to order plaintiff to discontinue setting up on its books any payments due under said contract or to make any such payments, and undertook to order plaintiff to make no payments to said Cities Service Gas Company for gas so purchased in excess of Twenty-nine and One-half (29½c) Cents per thousand cubic feet, hereinafter [fol. 10] called M. C. F., notwithstanding the fact that the contract between plaintiff and said Cities Service Gas Company requires the payment of 40 Cents per M. C. F. for all gas so purchased; and undertook to order plaintiff to reduce its rates to all its domestic customers in proportion to the reduction in expenses brought about by the attempted reduction in the price of purchased gas, pending a final determination as to what proper rates for plaintiff should be.

13

That being dissatisfied with said opinion, findings and order, plaintiff on July 30th, 1932, and within the time provided by law, filed with said Commission its application for a rehearing as required by law, a full, true and correct copy of which application is hereto attached, marked Exhibit "D," and made a part hereof.

14

That on August 5th, 1932, said application was by said Commission allowed as to paragraph 39 thereof and denied

as to the matters, reasons and grounds set out in the remaining 50 paragraphs of said application. A full, true and correct copy of said order granting a rehearing is hereto attached, marked Exhibit "E," and made a part hereof.

15

Pursuant to said order granting a rehearing, Exhibit "E", said Commission reopened said proceedings and set the same for further hearing on August 15th, 1932, at which time plaintiff appeared and introduced evidence as [fol. 11] to the earnings of the Cities Service Gas Company for the year ending June 30th, 1932, which was received by said Commission.

16

That on said rehearing so had on August 15th, 1932, plaintiff attempted to introduce other evidence in connection with other matters assigned and alleged as grounds for a rehearing in said application, Exhibit "E," but was wrongfully and unlawfully denied the right so to do, said Commission informing plaintiff that said rehearing was as to the allegations of paragraph 39 of plaintiff's said application, Exhibit "E," only, and that no evidence as to other matters alleged in said application, or relevant to other issues or features of said proceeding would be heard by said Commission, notwithstanding the contention of plaintiff and the fact that the Commission was without jurisdiction to grant a partial rehearing, and that plaintiff's application having been granted said proceedings were open for all purposes of the original hearings.

17

That upon the refusal of said Commission to permit witnesses to be sworn or testimony introduced concerning matters other than those alleged in paragraph 39 of plaintiff's said application, Exhibit "E," and the unlawful and wrongful denial by said Commission of plaintiff's right to introduce other evidence, plaintiff formally made offers to introduce evidence showing:

(a) That the present fair value of its property used and useful in rendering service to its consumers in the City of

Wichita, Kansas, was $2,872,854; that its gross earnings [fol. 12] for the year ending June 30th, 1932, were $1,818,850; that its net earnings applicable to depreciation and return for said period were $181,096; that if present salary reductions had been in effect for said entire period net earnings applicable to depreciation and return would have been $205,434, or 7.2 per cent on the present fair value of its property; that it could not purchase gas for domestic purposes for less than 40 cents per M. C. F. and that the reduction in plaintiff's rates attempted to be ordered in the Commission's order of July 20th, 1932, was unreasonable, unjust and would result in the confiscation of its property. A full, true and correct copy of said offer is hereto attached, marked Exhibit "F," and made a part hereof.

(b) That the gas reserves of the Cities Service Gas Company are not excessive and in the opinion of the officers of the company are necessary in order to guarantee service; that the reserves of 71,267 acres allowed by the Commission are not adequate; that said 71,267 acres do not have the reserves of gas available to Cities Service Gas Company which the Commission found; that during 1931 the total volume of gas taken from the Texas Panhandle field was 1,263,000,000 cubic feet per day, of which only 219,000,000 feet per day was taken by pipe lines, or approximately 17 per cent; that the gas not delivered to pipe lines was used in gasoline plants, carbon black plants, the production of oil or blown in the air, and will continue to be so used or wasted in the same proportions unless prohibited by lawful orders of the Texas Commission; that [fol. 13] said Commission now has under consideration an order limiting all takes from wells to 5 per cent of the open flow and an order shutting in all wells having unconnected offsets; that if the Texas Commission makes the proposed order and it is enforced the 71,267 acres allowed by this Commission will be wholly inadequate for even the coming winter and if the Cities Service Gas Company restricts its takes to the acreage allowed by this Commisson, service will fail; that under present practices in Texas the owners of approximately 10 per cent of the leases are producing approximately 82 per cent of the gas, none of which is connected to pipe lines or used by them; that rock pressure in certain areas has diminished from the original 430 pounds

to less than 50 pounds; that the gas in the area, including the 71,267 acres allowed by the Commission, is migrating to the low pressure area and will be lost to the pipe lines; that none of the gas reserves now owned and held by the Cities Service Gas Company was bought or is being held for speculation and that the Commission overestimated the amount of gas available to the Cities Service Gas Company from the 71,267 acres found by it to be sufficient. A full, true and correct copy of said offer is hereto attached, marked Exhibit "G," and made a part hereof.

(c) That the dry hole allowance of $12,000.00 per year fixed by said Commission in its order is wholly insufficient, unjust and unreasonable for the reason that in 1930 Cities Service Gas Company drilled ten dry holes at a cost of $174,748.00 and in 1931 drilled two dry holes at a cost of $126,339.00, and that it is impracticable to undertake any exploratory drilling with a limitation of $12,000.00 on the cost. A full, true and correct copy of said offer is hereto attached, marked Exhibit "H," and made a part hereof.

[fol. 14] (d) That the assumptions made by the Commission in its opinion, findings and order were not warranted in that rotary drilling is not generally used for gas wells in the fields where the wells of the Cities Service Gas Company are located and the expense of rotary drilling is greater than the cost of wells drilled with standard tools, all for the purpose of showing that the value found by the Commission of the gas wells of the Cities Service Gas Company was unreasonably low. A full, true and correct copy of said offer is hereto attached, marked Exhibit "I," and made a part hereof.

(e) That the present value of the property of all of the respondents (this plaintiff and nine other companies) in all of the cities served by them is $15,326,298.00; that their joint gross earnings for the year ending June 30th, 1932, were $7,092,398.00; that their net earnings applicable to depreciation and return for the same period were $665,233.00 subject to minor adjustments, and that had the present salary reductions been in effect for the entire period the net earnings would have been $756,989.00, or 4.9 per cent on the fair value of all of their properties. A full, true and correct copy of said offer is hereto attached, marked Exhibit "J," and made a part hereof.

18

That on August 31st, 1932, said Commission handed down its opinion on rehearing in which it added to the value of the property of the Cities Service Gas Company found by it as of September 1st, 1931, in its original opinion and findings, Exhibit "C," the sum of $119,275.00, and found said value to be as of September 1st, 1931, $73,148,510.00; that the net income of the Cities Service Gas Company for the year ending June 30th, 1932, amounted to [fol. 15] $7,861,516.85; that an item of $52,297.13 in the operating expenses of the Cities Service Gas Company representing payments made to Henry L. Doherty & Company should be disallowed; that an item of $50,000.00 in the operating expenses of the Cities Service Gas Company representing its expense in the proceedings before the Commission should be disallowed; that with both of said items deducted the net income before allowance for depreciation and depletion of the Cities Service Gas Company was the sum of $7,963,813.00; that allowances should be made for depreciation, depletion, amortization and dry hole expense aggregating $1,977,591.00; and that after such deductions the net income of the Cities Service Gas Company was for the year ending June 30th, 1932, $5,986,222.00, which the Commission finds is more than 8 per cent of the fair value of the property of the Cities Service Gas Company on September 1st, 1931, of $73,148,510.00, so found by said Commission (the exact percentage being 8.1837 per cent, and without the elimination of said item of $52,297.13, representing payments made to Henry L. Doherty & Company, and said item of $50,000.00, representing the expense of the proceding before said Commission, said percentage would have been 8.0438). A full, true and correct copy of said opinion on rehearing is hereto attached, marked Exhibit "K," and made a part hereof.

19

That in said opinion on rehearing, Exhibit "K," after finding the value of the property of the Cities Service Gas Company and the fact that during the year ending June 30th, 1932, it earned according to its actual experience only 8.0438 per cent on the value found by the Commis- [fol. 16] sion itself, and ignoring the fact that it had no

jurisdiction over the Cities Service Gas Company to fix its rates to be charged in interstate commerce, and ignoring the fact that it had under consideration only the reasonableness of the contract between the Cities Service Company and this plaintiff as of the time of said investigation, said Commission unlawfully and arbitrarily proceeded to find the average value of the property of the Cities Service Gas Company over a three year period, and the average depreciation and depletion requirements of said company over said period, and the average net income of the company over said period and in such manner arrived at the conclusion that a rate of 30 cents per M. C. F., if charged by the Cities Service Gas Company during said three year period, would have produced a return of 7 per cent on the average value of the property of said company during said period (the actual percentage being 6.98 per cent), all of which is pure speculation and conjecture and has no relevancy to the reasonableness or unreasonableness of said city gate contract at the present time.

20

That on the 31st day of August, 1932, and at the same time said Commission handed down its opinion on rehearing, it also issued an order directed to this plaintiff and to thirteen other companies joined with this plaintiff in said proceding in which it found that the contract between Henry L. Doherty & Company and this plaintiff under which this plaintiff pays to Henry L. Doherty & Company for services rendered by it one and three-fourths per cent of its gross revenues is unreasonable; that the contract between this plaintiff and the Cities Service Gas Company [fol. 17] under which it pays 40 cents for gas sold and delivered to it for domestic purposes is unreasonable in so far as it exceeds the 30-cent rate established by the Commission, and ordered that on and after September 1st, 1932, this plaintiff and all other respondents in said proceeding cease to set up on their books as an expense item any payment to Henry L. Doherty & Company under said contract requiring the payment of 1¾ per cent of their gross income or any payments made to Cities Service Gas Company for main line town border gas in excess of 30 cents per M. C. F. and that this plaintiff and its co-respondents in said proceeding before the Commission should give no

consideration to any such payments in fixing a rate for domestic consumers; that on October 17th, 1932, this plaintiff and its co-respondents in said proceeding before the Commission appear before said Commission and show cause why the reduction in expenses as set forth in said order should not be passed on to consumers with such other reductions as might be found reasonable. A full, true and correct copy of said order is hereto attached, marked Exhibit "L," and made a part hereof.

21

That on August 31st, 1932, and at the same time said Commission handed down its said opinion on rehearing, Exhibit "K," and its said order, Exhibit "L," and notwithstanding the fact that in said order, Exhibit "L," this plaintiff was ordered and directed to appear before said Commission on October 17th, 1932, and show cause why the reduction in its expenses occasioned by the elimination of the payment to Henry L. Doherty & Company and the reduction in the payment to the Cities Service Gas Company for gas purchased at the city gate should not be [fol. 18] passed on to its consumers, said Commission issued an order effective September 1st, 1932, and until a hearing is held and an order issued, that this plaintiff and its co-respondents in said proceeding before the Commission should charge rates to their respective consumers which would pass on to the consumers the different between what this plaintiff and its co-respondents in said proceeding are now paying the Cities Service Gas Company for gas at the city gate and the rate of 30 cents per M. C. F. found by said Commission. A full, true and correct copy of said order is hereto attached, marked Exhibit "M," and made a part hereof.

22

That on the 8th day of September, 1932, this plaintiff filed with said Commission its application for a rehearing, a full, true and correct copy of which application is hereto attached, marked Exhibit "N," and made a part hereof, and on September 9, 1932, filed a supplemental application for rehearing, hereto attached and marked Exhibit "O."

23

That said application and supplemental application for a rehearing, Exhibits "N" and "O," were by said Commission on the 12th day of September, 1932, denied.

24

That the orders so issued by said Commission on August 31st, 1932, Exhibits "L" and "M" hereto attached, in which said Commission finds unreasonable and refuses to recognize plaintiff's contract with Cities Service Gas Com- [fol. 19] pany for the purchase of its supply of gas at the city gate, its contract with Henry L. Doherty & Company under which plaintiff pays 1¾ per cent of its gross revenue for services rendered to it by said Henry L. Doherty & Company and said order purporting to put in effect as of September 1st, 1932, a reduction in rates of plaintiff on account of the disallowance by said Commission of items of its operating expense caused by the disapproval of said contracts, are unlawful, unreasonable and void because in direct violation of the Constitution and Laws of the State of Kansas and the Constitution and Laws of the United States, as hereinafter specified.

25

Contract with Cities Service Gas Company

That said orders of said Commission, and each and all of them, in so far as they purport to disapprove the contract entered into between plaintiff and the Cities Service Gas Company under the terms of which plaintiff pays to said Cities Service Gas Company the price of 40 cents per M. C. F. for gas sold and delivered to it at the city gate for domestic purposes and in so far as they and each of them purport to disallow as an item of plaintiff's operating expense any sum paid for purchased gas in excess of 30 cents per M. C. F., are unlawful, unreasonable, arbitrary and void for the following reasons:

(a) For the reason that in said opinions, findings and orders said Commission found the value of the property or rate base of the Cities Service Gas Company to be $73,148,510.00; that the earnings of said company for the year

ending June 30th, 1932, were $7,963,813.00 applicable to replacement reserves and return on the fair value of the [fol. 20] property; that replacement reserves for said period should be $1,977,591.00 and that the net income after reserves applicable to return on the value of said property was $5,986,222.00, which amounts to an earning of only 8.1837 per cent on said Commission's own rate base so found and said Commission's own allowance for replacement reserves, and an earning of only 8.0438 per cent if the sum of $52,297.13 wrongfully and unlawfully disallowed by said Commission as an item of operating expense on account of it being paid to Henry L. Doherty & Company and if the item of $50,000.00 wrongfully and unlawfully disallowed by said Commission as an item of operating expense for the reason that it represented expenses incurred in said proceedings before said Commission be included in expenses. And plaintiff alleges that said earning is less than a reasonable rate of return for said Cities Service Gas Company considering the unusual hazards of its business and is less than a return necessary to attract capital to said business at this time and under present conditions, it therefore being apparent on the face of said opinions, findings and orders that the contract between plaintiff and the Cities Service Gas Company is reasonable, does not indicate any absence of arm's length dealing between plaintiff and said company on account of their affiliation and should not have been disapproved.

(b) For the reason that the attempt of said Commission in said opinions, findings and orders, and each of them, to avoid the clear and undisputed reasonableness of the earnings of the said Cities Service Gas Company by averaging the earnings over a period of years and applying same to an average value of property, is unreasonable, unjust and unlawful and does not change or alter the Commission's finding that said Cities Service Gas Company [fol. 21] earned only 8.1837 per cent on the value of its property found by said Commission after deducting reserves approved by said Commission, said Commission having no jurisdiction, power or authority to determine the present reasonableness or unreasonableness of said contract on the property values and earnings of said Cities Service Gas Company as of any time other than the time said opinions, findings and orders were entered.

(c) For the reason that said opinions, findings and orders on their face show the contract between plaintiff and the Cities Service Gas Company to be such a contract as would have been entered into by parties unaffiliated dealing at arm's length and in the general and open market subject to the usual safeguards of bargaining and competition.

(d) For the reason that said Commission in dealing with the item of interest during construction, as appears in Exhibit "C," pages 78 and 79, found that 6 per cent was a proper rate to use for this item notwithstanding the fact that it is common knowledge of which the Court may take judicial notice that money could not be procured at the time of said hearing at such rate and notwithstanding the fact that the Commission found 7 per cent to be a proper rate of return for the Cities Service Gas Company after the completion of its plant and after the same was placed in operation, said Commission by adopting said 6 per cent having thereby eliminated from the rate base of the Cities Service Gas Company approximately one million dollars. . .

(e) For the reason that in its consideration of the item of going value as appears in Exhibit "C," pages 85 to 88, the Commission unlawfully, unreasonably, arbitrarily and capriciously allowed only the sum of $2,000,000.00 on its own valuation of $73,148,510.00 and ignored all the evi- [fol. 22] dence in the case on the subject, such evidence consisting of the testimony of F. C. Hamilton, engineer for plaintiff, that a proper allowance would be $8,898,532.00, and the testimony of its own witness, E. B. Black, that such value was $3,820,000.00, and ignored the uniform practice of courts and commissions to allow for such item approximately 10 per cent of the rate base, by which arbitrary and unreasonable action said Commission reduced the proper rate base of said Cities Service Gas Company over six million dollars.

(f) For the reason that said Commission in its consideration of the item of gas leases and reserves of said Cities Service Gas Company after finding that the present fair market value of such reserves was $6,279,237.00 and the present book value $6,573,489.70, as appears in Exhibit "C" at pages 99 and 100, unreasonably and arbitrarily found that most of said reserves were not used and useful

and allowed for said item only the sum of $2,874,390.00, thereby eliminating from the rate base of the Cities Service Gas Company the sum of $3,404,847.00, which on its own finding of present market value should have been included; and said Commission on rehearing wrongfully refused to permit plaintiff to show that the reserves allowed by said Commission were inadequate and would result in absolute failure of service as is shown by Exhibit "G" hereto attached. By all of which unreasonable, arbitrary and unwarranted conduct said Commission undertook, without one word of evidence from any witness in support of its finding as to what would constitute proper reserves for said Cities Service Gas Company, to substitute its own judgment and to usurp the duties of the officers of said company upon whom the responsibility for service rests.

[fol. 23] (g) For the reason that said Commission eliminated from the replacement reserves of the Cities Service Gas Company all lease rentals and development expense on leases which it wrongfully found to be not used and useful, amounting to the sum of $532,530.77, as appears from said order, Exhibit "C," at page 112, and also eliminated the reserve which must be accrued for amortizing the cost of said leases, amounting to $314,981.68, as appears from said order, Exhibit "C," page 112, or a total of $847,512.45.

(h) For the reason that said Commission, in determining the rate base of the Cities Service Gas Company, depreciated overheads, thereby eliminating from said rate base the sum of $1,011,392.00, without making any allowance in replacement reserves to compensate for such depreciation, which reserve should have been included in the amount of $30,443.00 annually, as appears by the opinion of said Commission, Exhibit "C," at page 111, or said overheads should not have been depreciated and said rate base should have been accordingly increased.

(i) For the reason that it is apparent on the face of said opinions, findings and orders that if said Commission had made proper allowances in the rate base of the Cities Service Gas Company for interest during construction, going value and leases and gas reserves, and had made reasonable allowances for replacement reserves, the rate base of said Cities Service Gas Company would be so in-

creased and its earnings after replacement reserves so decreased on the Commission's own findings that the present earnings of said company after reserves and applicable for return would amount to less than 6¼ per cent on such rate base.

(j) For the reason that said Cities Service Gas Com-
[fol. 24] pany is engaged in interstate commerce the right to control which is vested by the Constitution of the United States exclusively in Congress, and said Commission is without jurisdiction to fix a rate for said company or to proceed in the manner attempted in said proceedings so instituted by it or to make the orders herein set out.

(k) For the reason that the value of the property of the Cities Service Gas Company used and useful in carrying on its said business on August 31st, 1932, and at all times since that date, was and is not less than $105,857,402.00, and the finding by said Commission in said opinion and orders of August 31st, 1932, that said value was only the sum of $73,148,510.00 is unreasonable, unjust and contrary to all the evidence introduced before said Commission.

(l) For the reason that if the price of 30 cents for gas sold for domestic purposes at the city gate by the Cities Service Gas Company had been in effect during the year ending June 30th, 1932, and if said rate of 30 cents per M. C. F. is applied to the actual business transacted by said Cities Service Gas Company for said period, its gross earnings would have been reduced in the sum of $1,926,145.07 and its net earnings before replacement reserves would have been $5,935,371.78, which is a return of only 5.4 per cent on said Commission's own rate base as found in said opinion and orders of $73,148,510.00, which rate base is entirely unreasonable, unjust and inadequate as hereinbefore alleged after deducting the Commission's own unreasonable, unjust and inadequate allowance for replacement reserves, and if said rate had been so applied during said period the earnings of the Cities Service Gas Company would have amounted to only 5.6 per cent on the present fair value of its property of $105,857,402.00 for
[fol. 25] all the purposes of replacement reserves, depreciation, amortization, depletion and return.

(m) For the reason that in its consideration of the reasonableness of said contract between plaintiff and Cities Service Gas Company for plaintiff's supply of gas at the city gate it was the duty of said Commission, in the absence of any jurisdiction, power or authority over the interstate business of said company, to consider its operations, business and experience as the same actually existed and were being carried on by said company, without undertaking or attempting to determine the reasonableness or usefulness of its gas reserves or any other item of its property and without undertaking or attempting to determine the reasonableness of its operating expenses, or any item thereof, the jurisdiction of said Commission being limited to the determination of the reasonableness of such contract under existing operating conditions of the Cities Service Gas Company and said Commission being without jurisdiction, power or authority to regulate said company as attempted in said opinions, findings and orders.

(n) For the reason that said Commission has no jurisdiction, power or authority in a proceeding of the nature held by it and in the absence of any issue as to proper rates to be charged by this plaintiff to determine the moot question of the reasonableness of an item of plaintiff's operating expenses.

(o) For the reason that the finding of said Commission that the contract between plaintiff and Cities Service Gas Company was unreasonable and its order prohibiting plaintiff from setting up on its books any payments due under said contract and prohibiting plaintiff from taking such payments into consideration in fixing rates for its consumers is contrary to all evidence introduced before said [fol. 26] Commission in said proceedings and is entirely without support in the evidence.

(p) For the reason that the assumption of jurisdiction by said Commission in issuing the order for investigation, Exhibit "A," herein and all subsequent proceedings of said Commission under said order are in direct violation of Chapter 239 of the Session Laws of the State of Kansas of 1931 under which statute the right of the Commission to disapprove contracts and disallow items of operating expense is limited to proceedings, the purpose of which is to

ascertain the reasonableness of a rate or charge to be made by a public utility.

26

Contract with Henry L. Doherty & Company

Plaintiff further alleges that said opinion and orders of said Commission entered August 31st, 1932, and each and all of them, in so far as they purport to find unreasonable the contract between the plaintiff and Henry L. Doherty & Company under which plaintiff pays to said Henry L. Doherty & Company 1¾ per cent of its gross revenues, are unreasonable, unjust, unlawful and void for the following reasons:

(a) For the reason that said Commission has no jurisdiction, power or authority in a proceeding of the nature held by it and in the absence of any issue as to proper rates to be charged by this plaintiff to determine the moot question of the reasonableness of an item of plaintiff's operating expenses.

(b) For the reason that said Commission in said investigation so held by it did not have before it any evidence whatever as to the value of plaintiff's property used and useful in rendering the service in which it is engaged, [fol. 27] its operating experience or the reasonableness of its existing rates, and unlawfully, unreasonably and unjustly refused to permit plaintiff to introduce any such evidence and was therefore not in a position to determine whether or not the disallowance of said item of operating expense world affect the rates then being charged by plaintiff or warrant a decrease in rates to consumers.

(c) For the reason that said Commission was without jurisdiction, power or authority to disallow said item of plaintiff's operating expense in the absence of an express finding that existing rates were unreasonable by reason of the inclusion of said item in plaintiff's operating expenses and the substitution of a new rate in lieu of the old rate so found to be unreasonable.

(d) For the reason that plaintiff offered to show to said Commission in said original proceeding and on rehearing,

as shown by Exhibit "F" hereto attached, that under existing rates it was earning only 7.2 per cent on the present fair value of its property, and the disallowance of said item in plaintiff's operating expenses could not possibly affect the reasonableness of its existing rates or give jurisdiction to the Commission to reduce the same on account of the disallowance of said item.

(e) For the reason that said Commission by disapproving and disallowing a contract entered into by the officers and directors of plaintiff in accordance with their business judgment has unlawfully and unreasonably undertaken the management of plaintiff's property and has undertaken to substitute its judgment for the judgment of the officers and directors of plaintiff in regard to a matter of business policy.

(f) For the reason that the finding of said Commis-
[fol. 28] sion that the contract between plaintiff and Henry L. Doherty & Company was unreasonable and its order prohibiting plaintiff from setting up on its books any payments due under said contract and prohibiting plaintiff from taking such payments into consideration in fixing rates for its consumers is contrary to all evidence introduced before said Commission in said proceeding and is entirely without support in the evidence, while in truth and fact services of great value were and are being rendered by said Henry L. Doherty & Company, to-wit, the amount charged.

27

Reduction in Rates

Plaintiff further alleges that said orders of said Commission herein recited and set out and each and all of them, in so far as they purport to change, alter and reduce the rates of this plaintiff to be charged by it to its consumers, are unreasonable, unlawful, arbitrary and void for the following reasons:

(a) For the reason that said orders, and each of them, and particularly said order, Exhibit "M," directing this plaintiff to reduce its rates to consumers as of September 1st, 1932, is in direct violation of Section 66-115, Re-

vised Statutes of Kansas of 1923, which statute expressly provides that all orders of said Commission "shall be in force and effect on and after 30 days from the making thereof."

(b) For the reason that this plaintiff was unlawfully, unreasonably and arbitrarily denied an opporunity to present to said Commission evidence as to the value of its property, its earnings and its general operating experience un- [fol. 29] der the rates now being charged by it, and to show to said Commission that for the year ending June 30th, 1932, its earnings under existing rates produced a return of only 7.2 per cent on the present fair value of its property, said 7.2 per cent being the earnings of said company for said period for both depreciation and return, and to show that any reduction in existing rates would be unreasonable, unjust and would result in the confiscation of its property, all of which this plaintiff offered and demanded the opportunity to show as is set out in Exhibit "F," hereto attached.

(c) For the reason that the Commission did not investigate the reasonableness of the existing rates of this plaintiff, did not have before it any evidence as to the value of plaintiff's property or any evidence as to its operating experience, or make any investigation whatever as to any such matters, or any other matters concerning the reasonableness of its present rates, as required by Sections 66-110 and 66-113, Revised Statutes of Kansas of 1923, and other statutes of the State of Kansas, such investigation being required before such Commission has any jurisdiction, power or authority whatever over the rates of this plaintiff and its jurisdiction to act in the premises being entirely dependent upon a previous investigation of relevent facts.

(d) For the reason that said Commission did not find the existing rates of this plaintiff to be unjust, unreasonable, unjustly discriminatory, or unduly preferential, or otherwise in violation of the statutes of the State of Kansas, as is expressly required by Section 66-110 and Section 66-113, Revised Statutes of Kansas of 1923, and other sections of said Act, and had before it no evidence upon which any such finding could have been made, and [fol. 30] for the reason that in the absence of such finding

said Commission is without any jurisdiction, power or authority to change, alter or amend in any manner the existing rates of this plaintiff.

(e) For the reason that said Commission did not fix and order substituted for the present rates of this plaintiff any other or different rate as is required by Section 66-110, Revised Statutes of 1923, and other laws of the State of Kansas, but merely undertook to order this plaintiff to pass on to its consumers a theoretical saving in its expenses in an amount undetermined and impossible of determination and which amount varies in accordance with the variation in business transacted by this plaintiff on each and every day of its operation, such order being in said respect so ambiguous, indefinite and meaningless as to be impossible of performance.

(f) For the reason that the existing rate of plaintiff established by order of said Commission consists of a charge of .145 per 100 cu. ft. for 1st 1,000 cu. ft. per month, .095 per 100 cu. ft. for next 2,500 cu. ft. per month, .05 per 100 cu. ft. for next 146,500 cu. ft. per month; .023 per 100 cu. ft. for balance of monthly delivery that the form of said rate is such that even a determined and definite reduction to be passed on to consumers could not be applied thereto without a direction as to which step or block in said rate should be charged and how said reduction should be spread over the monthly consumption of any customer, said order being in said respect so indefinite and ambiguous as to be impossible of performance.

(g) For the reason that said Commission without investigation, without finding the unreasonableness of existing rates and without affording plaintiff its day in court, [fol. 31], or an opportunty to be heard, undertook to order a reduction in existing rates immediately effective and to then at a later time hold such proceeding as is required by law in the first instance for the purpose of determining whether its previous order reducing rates should have been made and entered, thereby requiring plaintiff to suffer the confiscation of its property during the entire rate making period.

(h) For the reason that plaintiff has been notified by the Cities Service Gas Company that it will not recognize the order of said Commission and will not sell and deliver gas

to plaintiff for domestic purposes at a less price than 40 cents per M. C. F. at the city gate and if plaintiff should reduce its rates to consumers at this time and as required by said order, it would be placed in the position of guaranteeing the validity of said order and in the event the same should be held to be unlawful, unreasonable or set aside for any other reason, this plaintiff would be irreparably injured and damaged for the reason that it could not recoup from its consumers the loss it would sustain in the event said Cities Service Gas Company should compel it to pay 40 cents per M. C. F. for the gas so sold and delivered to it.

(i) For the reason that said Commission has no jurisdiction, power or authority in a proceeding of the nature held by it and in the absence of any issue as to proper rates to be charged by this plaintiff to determine the moot question of the reasonableness of an item of plaintiff's operating expense.

(j) For the reason that the assumption of jurisdiction by said Commission in issuing the order for investigation, Exhibit "A", herein and all subsequent proceedings of said [fol. 32] Commission under said order are in direct violation of Chapter 239 of the Session Laws of the State of Kansas of 1931 under which statute the right of the Commission to disapprove contracts and disallow items of operating expense is limited to proceedings, the purpose of which is to ascertain the reasonableness of a rate or charge to be made by a public utility.

(k) For the reason that said Commission, by disapproving and disallowing a contract entered into by the officers and directors of plaintiff in accordance with their business judgment, has unlawfully and unreasonably undertaken the management of plantiff's property and has undertaken to substitute its judgment for the judgment of the officers and directors of plaintiff in regard to a matter of business policy.

28

Plaintiff further alleges that said defendant Commission was without jurisdiction, power or authority to proceed against utilities generally in one joint proceeding and to compel plaintiff to have joined with it others with which it had nothing in common; that the entire proceeding had before said Commission was beyond its jurisdiction; that

plaintiff was unlawfully and wrongfully compelled to appear before said Commission and that the objections of the plaintiff as set out in Exhibit "B" should have been sustained.

29

Plaintiff further alleges that for all of the reasons hereinbefore set out said proceedings before said Commission and all opinions, findings and orders made by it therein are unreasonable, unjust, unlawful and void in that they deprive [fol. 33] plaintiff of its property without due process of law; deny it the equal protection of the law; impair the obligation of its contracts; undertake to legislate with respect to interstate commerce and usurp the business management of the plaintiff company, all in violation of the Constitution and laws of the United States and of the State of Kansas, and particularly Clause 3 of Section 8 of Article 1, the first subdivision of Section 10 of Article 1 of the Constitution of the United States and the Fourteenth Amendment thereto.

30

That plaintiff cannot procure gas for the requirements of its business from the Cities Service Gas Company for less than 40 cents per M. C. F. and if it is, by said orders of said Commission, compelled to pay said sum for purchased gas and base its rates to consumers on a price of 30 cents per M. C. F., it cannot make a fair or reasonable return on the fair value of its property, and its property will be confiscated, all of which is in violation of and repugnant to the Constitution and Laws of the United States as alleged in the next preceding paragraph hereof.

31

Plaintiff alleges that it is the intention and purpose of said defendants to attempt to intimidate plaintiff into the acceptance of said orders of August 31st, 1932, by instituting proceedings against plaintiff and its correspondents in said proceeding before the Commission for the appointment of receivers for their several properties, and under date of September 16th, 1932, in pursuance of said intention [fol. 34] and purpose and at the instigation of said defendant, The Public Service Commission, the Governor of the State of Kansas ordered the defendant Roland Boynton,

Attorney General of said state, to institute court proceedings seeking dissolution of said several companies and the appointment of receivers for them and said Attorney General has stated that he will obey the directions of said Governor; that the effect of the filing of such proceedings will be to adversely affect plaintiff's public relations, destroy confidence of its stockholders, affect its financial standing and otherwise embarrass it, and will affect its ability to render service to its consumers; that the purpose of said proceedings is to intimidate and coerce plaintiff into the acceptance of said orders and also to take the conduct of plaintiff's business out of the hands of its officers and prevent it from contesting said orders in this or any other court; that plaintiff has never been requested or directed by said defendants or any other officer of the State of Kansas to transact its business in any manner different from that in which it is now being conducted and plaintiff stands ready and willing at any time to comply with the lawful orders or directions of any court or officer respecting any of its corporate practices; that without regard to plaintiff's ability to defend itself in any such proceedings if brought, the filing of such charges and consequent publicity will cause it irreparable damage and injury.

32

Plaintiff further alleges that in its supplemental application for a rehearing, Exhibit "O" herein, it called to the attention of said defendant Commission the fact that a certain order had been issued by the regulatory body of the [fol. 35] State of Texas having jurisdiction in the premises restricting the amount of gas which said Cities Service Gas Company could take from wells on its gas reserves to 4 per cent of the potential capacity of such wells, which application was by said Commission denied as shown by its order of September 12th, 1932, as being without merit for the reason as plaintiff is informed and believes, that said defendant Commission after communication with said regulatory body of the State of Texas was informed that said restriction of 4 per cent did not apply to the requirements of pipe lines for domestic and industrial use; that plaintiff is informed that on September 16th, 1932, said regulatory body of the State of Texas amended its original order so as to eliminate from its restriction of 4 per cent gas used for

domestic and industrial purposes, leaving said restriction as an absolute and unqualified limitation on the takes from all wells in the gas reserves of the Cities Service Gas Company, thereby making the gas reserves allowed by said Commission as herein before set out entirely inadequate, insufficient and unreasonable.

33

Plaintiff is without adequate remedy at law in the premises herein before set forth and will suffer irreparable injury unless accorded the injunctive relief herein prayed for; that the penalties provided for the infraction of orders of said Commission are so enormous, cruel and unusual as to intimidate plantiff and to force it to abandon any rights it may have to act independently thereof; that plaintiff will be unable to make collection from its consumers for gas sold and delivered to them if it attempts to act contrary to said orders and in the absence of the relief herein prayed [fol. 36] for plaintiff is unable to protect itself against the same.

Wherefore, since plaintiff is without adequate remedy save in a court of equity, it prays:

(A) That the said defendants, and each of them and all persons acting through or under them, be permanently restrained and enjoined from the enforcement of said orders of August 31st, 1932, or from interfering with the existing rates of plaintiff or its contracts with Henry L. Doherty & Company and Cities Service Gas Company by reason of said orders, or either of them, and from commencing, instituting or prosecuting in this or any other court or tribunal any suit or proceeding to litigate any of the matters herein complained of or the purpose of which is to compel or intimidate plaintiff to accept said orders or deprive it of its right to prosecute this or any other proceeding to contest the validity of said orders.

(B) That this cause be set for hearing on application for temporary injunction at an early date and that upon said hearing the court issue its temporary injunction enjoining said defendants, and each of them, from the enforcement of said orders and that pending said hearing the court enter its restraining order with like effect.

(C) That the plaintiff have such other and further relief as may be just and equitable.

(D) That there be issued out of this Court a writ of subpœna to be served upon the defendants, The Public Service Commission of the State of Kansas and Jesse W. Greenleaf, Thurman Hill and C. W. Campbell as members of said Commission, and Roland Boynton, Attorney General of the State of Kansas, thereby commanding them, and each of them, at a certain time and under a certain penalty therein to be limited, personally to appear before this Honorable Court and then and there full, true, direct [fol. 37] and perfect answer make to all and singular in the premises and further to stand to perform and abide such further order, direction and decree therein as shall seem agreeable to equity and good conscience; and your plaintiff will ever pray.

Robt. D. Garver, Robert Stone, Attorneys for Plaintiff.

Duly sworn to by Robert D. Garver. Jurat omitted in printing.

[fol. 38] EXHIBIT "A" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Part A. Wichita Gas Co., Wichita;
" B. Hutchinson Gas Co., Hutchinson;
" C. Newton Gas Co., Newton;
" D. Pittsburg Gas Co., Pittsburg;
" E. Capital Gas & Electric Co., Topeka;
" F. Wyandotte Gas Co., Kansas City, Kansas;
" G. Arkansas Valley Gas Co., Arkansas City;
" H. Girard Gas Co., Girard;
" I. Union Public Service Co., 45 Towns;
" J. Western Dist. Co., 27 Towns;

" K. Winfield Natural Gas Co., Winfield;
" L. Tri-City Gas Co. a/c Gas Service Co., Kansas City, Mo.;
" M. Gas Service Co., Kansas City, Mo.;
" N. American Pipe Line Co., Bartlesville, Okla.,

Respondents.

Order for Investigation

Now on this second day of July, 1931, it appears to the Public Service Commission for the State of Kansas, that the reasonableness of all contracts, and charges made by holding companies to subsidiary companies of the Cities Service Company (respondents above named) operating within the State of Kansas, should be inquired into for the [fol. 39] purpose of determining the reasonableness of such contracts and the reasonableness of the charges made for services and commodities furnished.

It further appears to the Public Service Commission that the holding companies of the said subsidiary companies occupy a special position with particular advantages in relation to the sale of gas and contracts for service and commodities furnished; and that the holding companies through stock ownership dominate and control the management of the said subsidiary companies.

The Commission therefore finds that the contracts made and charges for services rendered and commodities furnished to said subsidiary distributing companies by the holding companies and Henry L. Doherty & Company should be inquired into to determine their reasonableness and to find what amount should be allocated in this respect to the operating expense of the subsidiary companies.

It is therefore by the Commission ordered: That an investigation be set for hearing on the 18th day of August, 1931, at 10 o'clock a. m., at the office of the Commission in Topeka, Kansas, to inquire into the reasonableness of contracts made with, and the services rendered to, the subsidiary companies of the Cities Service Company by their various holding companies.

It is further by the Commission ordered: That each of the above-named respondents appear on the above-mentioned date to give to the Commission such information as they may desire on their own behalf, and as may be required by the Commission, in behalf of said investigation, and to show

cause why such holding company contracts, or service or commodity charges, should they be found to be unreasonable, should not be disallowed as operating expense of the [fol. 40] distributing companies, and adjustment made in this respect as to charges made to the consumers.

By the Commission it is so ordered.

J. W. Greenleaf, Thurman Hill, Chas. W. Campbell, Commissioners. Attest: C. H. Benson, Secretary.

EXHIBIT "B" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges made by Holding Companies to Subsidiary Companies of the Cities Service Company

Entry of Appearance and Objections of The Wichita Gas Company

Comes now The Wichita Gas Company, a Kansas corporation, in compliance with the order of this Commission herein dated July 2nd, 1931, and hereby enters its appearance for the purpose of furnishing to this Commission all information which it has or is able to procure in regard to the contracts recited in said order.

Said respondent hereby expressly limits its appearance and appears specially for said purposes and said purposes only hereby expressly objecting to any consideration by this Commission in this proceeding of the reasonableness [fol. 41] or unreasonableness of its existing rates or any attempt to change the same by reason of any findings which this Commission may make in respect to said contracts from the evidence introduced herein and expressly denying the jurisdiction of the Commission to consider in this proceeding any issue as to the value of respondent's property, the adequacy or inadequacy of its earnings or the reasonableness or unreasonableness of its rates for the following reasons:

1. That the Commission has no juridiction, power or authority, under the laws of the State of Kansas, to proceed against utilities generally in one joint proceeding and to compel one utility to have joined with it others with which it has nothing in common.

2. That this respondent owns and operates a public utility only in the City of Topeka, Kansas, and its immediate environs, and its rates are, by law, required to be determined with respect to the value of its property used and useful in rendering its public service and without regard to the value of the properties of the other utilities joined herein.

3. That the other parties respondent to this proceeding are improperly joined with the respondent and are not necessary or proper parties as far as any proceeding against this respondent is concerned which involves a consideration of its rates.

4. That each public utility and each respondent herein as to each property which it operates is entitled, under the law, to a full, complete and separate hearing as to each such city or community and the rates as to each such city or community must be considered by this Commission separate and apart and without regard to the property or rates of any other utility.

5. That it will be impossible, in this proceeding, for any [fol. 42] utility to make a record covering proceedings affecting it without including therein proceedings concerning other utilities and impossible for such utility to avail itself of the right of appeal or review provided by law.

6. That each utility respondent herein is deprived of the right to conduct its cause according to its independent judgment and in a legal and orderly manner and to avail itself of the rights granted and guaranteed by the Constitution and Laws of the United States and of the State of Kansas.

7. That the existing rates of this respondent are inadequate, unremunerative and confiscatory in that they do not enable respondent to earn a fair return for all purposes on the fair value of its property and that no change in such rates can lawfully be made without affording respond-

ent an opportunity to present all pertinent facts relating to the value of its property and its financial experience, which opportunity cannot be adequately afforded in this proceeding wherein respondent is joined with utilities operating in some one hundred and eighty towns and communities, the rates for each of which must be determined by considerations entirely independent of every other property.

The Wichita Gas Company, by Robt. D. Garver, Robert Stone, Attorneys.

[fol. 43] EXHIBIT "D" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS

No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Application of the Wichita Gas Company for Rehearing

Comes now The Wichita Gas Company, one of the parties to the above proceeding, and fully reserving all its rights, as set out in its special appearance filed herein at the inception of this matter, applies for a rehearing in respect to all matters found and ordered and purported to have been determined herein by this Commission for the reason that its decision, findings and order, severally and collectively, are unlawful, unjust and unreasonable in the following respects and for the following reasons:

1

For the reason that in its investigation of the contract between the respondents and the Cities Service Gas Company for the supply of gas at the city gates of the respective cities served by respondents, the Commission has approached all questions involved the same as if it had power and jurisdiction under the law to fix the rates and commodity charges of the Cities Service Gas Company, a

corporation engaged in interstate commerce, and has, in effect, undertaken to fix the rates and commodity charges [fol. 44] of said interstate company in relation to its interstate business and has undertaken to and has fixed the rates and commodity charges for said company, the authority to do which is, by the Constitution of the United States, vested exclusively in the Congress of the United States, and by its decision and order said Commission has usurped the exclusive power of Congress and has acted wholly without legal authority, power or jurisdiction.

2

For the reason that the gas purchased by said respondents respectively at their respective city gates is natural gas transported by the Cities Service Gas Company in interstate commerce, national in its character, and said Cities Service Gas Company is lawfully entitled to sell said gas to the several respondents herein and to other like purchasers in the several states through which its transportation system passes without interference by the Commissions of the several state in which such interstate transaction is carried on and said decision, opinion, findings and order unlawfully deprive said Cities Service Gas Company of the fruits of said interstate transportation and unlawfully deny to it the free right to sell from its said transportation system its product so transported and unlawfully deprive it of the rights guaranteed to it by Clause 3 of Section 8 of Article 1 of the Constitution of the United States.

3

For that reason that said decision, opinion, findings and order, severally and collectively, and every part thereof, are in violation of Clause 3 of Section 8 of Article 1 of the [fol. 45] Constitution of the United States in that they seek to impose an unreasonable regulation and an undue burden on intertsate commerce, national in character, that can be imposed only by the Congress of the United States.

4

For the reason that said decision, opinion, findings and order are in violation of the first subdivision of Section 10 of Article 1 of the Constitution of the United States

in that they, and each of them, impair the obligation of the contracts of the Cities Service Gas Company and the contracts of this and the other respondents.

5

For the reason that said decision, opinion, findings and order, and every part thereof, are in violation of the Fourteenth Amendment to the Constitution of the United States in that they deprive Cities Service Gas Company and the respondents, and each of them, of their property without due process of law, destroy their freedom of contract and deny to them the equal protection of the law.

6

For the reason that the rate found by said Commission to be a reasonable price to be paid for gas at the gates of the cities supplied by respondents, respectively, is a rate that would not produce a reasonable return on the fair value of the property of the Cities Service Gas Company used and useful in such service; would result in the confiscation of its property and deprive it of its property without due process of law, all in violation of the Constitu- [fol. 46] tion of the United States and the laws and Constitution of the State of Kansas.

7

For the reason that the Cities Service Gas Company, in the sale of its product so transported in interstate commerce, national in character, is limited to the market connected with its transportation system, as now located, and that by its order to the several respondents herein it, in effect, deprives said Cities Service Gas Company of all market for its gas at rates other than those attempted to be established by said Commission in said decision, opinion, findings and order and deprives it of the right to carry on its business and deprives it of its property without due process of law, all in violation of the Constitution of the United States.

8

For the reason that said decision, opinion, findings and order in so far as they relate to the contract between this

respondent and Henry L. Doherty & Company and under which this respondent pays to Henry L. Doherty & Company 1¾ per cent of its gross revenue in compensation for the services rendered by said Henry L. Doherty & Company, impair the obligation of such contract; deny to respondent and to said Henry L. Doherty & Company the free right of contract; undertake the business management of the respondent company; usurp the duties of the officers and directors of said companies, respectively, and substitute the opinion and conclusion of said Commission for the business judgment of the officers and directors of said companies as to matters of purely business policy, all in viola- [fol. 47] tion of the Constitution of the United States and the Constitution and laws of the State of Kansas.

9

For the reason that said decision, opinion, findings and order, in so far as they relate to the contract between this respondent and Cities Service Gas Company and under which this respondent purchases its supply of gas for distribution to its consumers, impair the obligation of such contract; deny to respondent and to said Cities Service Gas Company the free right of contract; undertake the business management of the respondent company and the Cities Service Gas Company; usurp the duties of the officers and directors of said companies, respectively, and substitute the opinion and conclusions of said Commission for the business judgment of the officers and directors of said companies as to matters of purely business policy, all in violation of the Constitution of the United States and the Constitution and laws of the State of Kansas.

10

For the reason that said respondent has been informed and notified by said Cities Service Gas Company that it will not supply it with gas at the rate prescribed by said Commission in its said decision, opinion, findings and order; that respondent is without any other supply of gas with which to perform the public service in which it is engaged and that if said decision, opinion, findings and order become effective its ability to render service will be destroyed and it will have to discontinue service entirely.

[fol. 48] 11

For the reason that said decision, opinion, findings and order undertake to compel respondents, and each of them, as of August 1st, 1932, to pass on to their respective consumers a reduction of ten cents per 1,000 cubic feet, without an opportunity to be heard in the manner provided by the statutes of the State of Kansas or otherwise as to whether or not their rates would be reasonable and lawful in the event such reduction should be made as ordered.

12

For the reason that this respondent is now operating under insufficient and confiscatory rates and even if a reduction in its expenses could be effected, as provided in said decision, opinion, findings and order, the rates of respondent would still not be unreasonably high and would be less than it is entitled to lawfully charge.

13

For the reason that in the course of this proceeding said Commission refused to permit this respondent to show the present fair value of its property used and useful in rendering the service in which it is engaged and its financial experience under the rates now in effect, evidence in respect to which was offered by respondent in an effort to show that even if a reduction in the city gate rate should be ordered by the Commission its existing rates would not be affected, said Commission in that connection having informed respondent in open court that no such reduction was contemplated or would be attempted in any order which might be made as the result of said proceedings, by [fol. 49] which conduct of the Commission respondent was misled, misinformed and dec-ived as to the issue before said Commission, was deprived of a lawful hearing and was denied the opportunity of presenting their evidence.

14

For the reason that said decision, opinion, findings and order, in so far as they purport to order a reduction in the

rates charged by this respondent, are not supported by any evidence whatever as to the value of the property of this respondent, its financial experience or any other fact or evidence which would enable the commission to determine reasonable rates for it to put into effect.

15

For the reason that said Commission is entirely without jurisdiction to change, alter, or in any manner affect the rates being charged by respondent without a finding based on substantial evidence that the present rates of respondent are unreasonable or unlawful and no such finding has been made in this proceeding.

16

For the reason that said decision, opinion, findings and order undertake to put in effect reduced rates as of August 1st, 1932, prior to the time this application for rehearing, made mandatory under the statutes of Kansas and a condition precedent to any action in the courts attacking said decision, opinion, findings and order, can be submitted or passed upon by said Commission, whereby respondent is deprived of remedies afforded by the statutes of the State of Kansas for its protection.

[fol. 50] 17

For the reason that said decision, opinion, findings and order, and each of them and all parts thereof, are unsupported by the evidence and are contrary to the evidence.

18

For the reason that said decision, opinion, findings and order, and each of them and all parts thereof, are unreasonable, unjust and contrary to law.

19

For the reason that said decision, opinion, findings and order result in an unreasonable, unjust and unlawful discrimination in that they permit companies not affiliated with the Cities Service Gas Company to purchase their

supply of gas from the Cities Service Gas Company at a rate different from any permitted to be paid by respondent.

20

For the reason that in its said decision, opinion, findings and order the Commission erroneously attempted to average values and earnings over certain periods of time and by its failure to include certain items of property in use at a given time computed earnings on a much lower rate base than actually existed, thereby arriving at an entirely erroneous conclusion; that at the present time a full year's financial experience can be had on all property comprising the rate base of the Cities Service Gas Company and respondent asks an opportunity to make such showing, thereby eliminating all necessity for speculation and conjecture.

[fol. 51]

21

For the reason that there has been a change in conditions since the periods which the Commission considered in the hearings had herein so marked and exceptional as to constitute "the outstanding contemporary fact, dominating thought and action throughout the country" and of which the Commission must take judicial notice (284 U. S. 248) and such changed conditions have made the past financial experience of the Cities Service Gas Company, as shown by the evidence herein, no further applicable, competent or relevant.

22

For the reason that the valuation of the property of the Cities Service Gas Company used in its purported rate base is not the value of said property as of the date of said hearing, or the date agreed upon.

23

For the reason that the earnings of said Cities Service Gas Company found by said Commission to have been earned on the rate base found by it are not the earnings being made at the time of said hearings, or the date agreed upon.

24

For the reason that the earnings of the Cities Service Gas Company, at the time of said hearings, were not in excess of a reasonable return on the then fair value of its property.

[fol. 52]

25

For the reason that the Commission unlawfully and unreasonably usurped the prerogatives, duties and authority of the officers and directors of Cities Service Gas Company, upon whom the responsibility for service rests, and arbitrarily and unlawfully refused to include in the rate base of said company and in the value of its property leases of the value of many millions of dollars for the reason that said leases were not, in the opinion of said Commission, presently used or useful, such action of the Commission being wholly unsupported by any evidence and being entirely arbitrary.

26

For the reason that this respondent, in entering into its contract with the Cities Service Gas Company for its supply of gas, relied upon the gas reserves of said Cities Service Gas Company as then and now owned and controlled by it and contracted with respect to such reserves which, in the opinion of this respondent, were necessary to secure an adequate and lasting supply of gas and guarantee service to its consumers.

27

For the reason that said Commission eliminated from the operating expenses of Cities Service Gas Company rentals on leases which, in the business judgment of the officers of said company and of this respondent, are necessary to constitute adequate, proper and necessary gas reserves for its system, thereby unreasonably and unlawfully substituting their opinions and conclusions for the business judgment of the officers and directors of said [fol. 53] companies, such opinions and conclusions being wholly without support in the evidence.

28

For the reason that said Commission eliminated from the operating expenses of Cities Service Gas Company all

sums paid by it to Henry L. Doherty & Company as representing 1¾ per cent of its gross receipts from gas sold by it to unaffiliated distributing companies and other purchasers, said Commission having no jurisdiction, authority or power whatever over such contracts, its sole jurisdiction being dependent upon affiliation or the absence of arm's length dealing and also for the reason that said contract as between this respondent and Henry L. Doherty & Company was disapproved by the Commission on the basis that the services rendered by Henry L. Doherty & Company were a duplication of services rendered by The Gas Service Company whereas no services are rendered by The Gas Service Company to the Cities Service Gas Company or to unaffiliated distribution companies or to any other purchasers of gas from the Cities Service Gas Company and no such duplication could exist as to such contracts.

29

For the reason that the value found by said Commission of the property of the Cities Service Gas Company entirely ignores all testimony and evidence introduced before said Commission, including the state's own witnesses and is contrary to all evidence in the case.

[fol. 54] 30

For the reason that in its allowance of replacement reserves the Commission arbitrarily disregarded the only evidence in the case, which was the testimony of witnesses for respondents as to proper reserves for the Cities Service Gas Company, determined by the actual past experience of the company and the business judgment of its officers and directors to be proper, and in lieu thereof and without any support whatever in the evidence allowed an amount for replacement reserves based on the percentages which the reserves testified to by respondents' witnesses happen to bear to the value of the property of Cities Service Gas Company as claimed by it and as testified to by respondents' witnesses and applied such percentages so obtained to the erroneous value found by it for a part only of the property of the Cities Service Gas Company, which value is contrary to all evidence before the Commission, and the reserves so determined and allowed are entirely inadequate for the purposes intended.

31

For the reason that in a proceeding involving only the reasonableness of a contract for purchased gas the decision, opinion, findings and order of the Commission are un-*un*reasonable, unjust and unlawful in limiting said Cities Service Gas Company to a return of seven per cent after replacement reserves, such allowance being contrary to all evidence in the case and entirely inadequate under present economic conditions, a reasonable return as shown by the evidence being eight per cent and there being no evidence to the contrary.

[fol. 55]

32

For the reason that the decision, opinion, findings and order of the Commission, in so far as they purport to determine whether rates of the several respondents should be reduced and order a reduction thereof, are unreasonable, unlawful and void as not properly within the issues framed by the original order initiating this investigation and are contrary to the express statement of the issues by the Commission and its attorneys in open court (R. 8, 2859 to 2867, inc.) to the effect that if a reduction in the city gate rate should be ordered an opportunity would be given all distributing companies, respondents herein, including this respondent, to separately show the value of their property and their financial experience under existing rates before such rates would be changed.

33

For the reason that the Commission is without power, authority or jurisdiction to order a change in the rates of this respondent without the statutory notice that such change in rates is in issue and without affording the respondent an opportunity to present evidence showing the value of its property and its experience under existing rates, and for the reason that said order is made effective August 1st, 1932, contrary to law.

34

For the reason that the order of the Commission directing a reduction in the rates of this respondent as of August 1st, 1932, with the further order that respond-

ent appear on September 1st, 1932, to show cause why the reduction ordered should not be permanently con-
[fol. 56] tinued in effect, is unreasonable, unlawful, beyond the power and jurisdiction of the Commission and void for the reason that it would compel the respondent to suffer confiscation during the rate making period and for the reason that said order to show cause on September 1st is, in effect, an admission that the rate reductions ordered were made without a consideration of the necessary facts by the Commission and without an opportunity having been afforded this respondent to be heard on the issue as to whether or not its rates should be reduced.

35

For the reason that the order to show cause on September 1st, 1932, as to why a rate reduction should not be made permanent requires the respondents to be prepared on complete rate cases, including detailed valuations and financial studies and exhibits for ten companies doing business in almost one hundred separate cities and communities and involving property of the value of approximately $15,000,000.00, the preparation of which cases in the proper manner would require at least a year's time and the orderly and proper hearings of which matters would require months, all of which is physically impossible of performance on September 1st, 1932, and the result of said order would be that said reductions in rates so made without any issue being raised, evidence introduced or opportunity afforded for a hearing would be in effect for perhaps several years during which time respondents, and each of them, would be unlawfully deprived of a fair earning on the fair value of their properties respectively and their properties would be confiscated, taken without due process of law and they, and each of them, would be denied [fol. 57] the equal protection of the law, all in violation of the laws and Constitution of the State of Kansas and the Constitution of the United States.

36

For the reason that if the parts of said decision, opinion, findings and order directed to these respondents and calling for and ordering a reduction in their respective rates should be eliminated from said order there would remain

only a determination of the moot question as to the value of the property of the Cities Service Gas Company and an unlawful determination of what its rates should be at the several city gates, the right to determine which rests exclusively in the Congress of the United States and is wholly without the jurisdiction of this Commission.

37

For the reason that the Commission in its decision, opinion, findings and order did not value the property of the Cities Service Gas Company as of the time of said proceedings but erroneously attempted to arrive at an average value which does not represent the value of the property of said company at any certain time.

38

For the reason that the Commission in its said decision, opinion, findings and order did not ascertain the earnings of the Cities Service Gas Company as of the time of said proceedings or as of any definite time but erroneously undertook to average the same over a period of years, thereby arriving at an erroneous conclusion as to earnings which has no proper relation to the value of the property of the Cities Service Gas Company.

[fol. 58] 39.

For the reason that figures are now available showing the financial experience of the Cities Service Gas Company for the year ending June 30th, 1932, which figures were not available at the time of the several hearings herein or at the time said hearings were concluded, such presently available figures and experience show that the net earnings of the Cities Service Gas Company for all purposes and before replacement reserves were $7,865,110.82 for the year ending June 30th, 1932; that in its said decision, opinion, findings and order the Commission found a rate base for the Cities Service Gas Company as of September 1st, 1931, of $73,073,713.00 and further found that said company was entitled to earn thereon 7 per cent for return and approximately 3 per cent for replacement reserves, or a total of approximately ten per cent, or $7,087,751.00; that if the rate of 29½ cents per thou-

sand cubic feet, found by the Commission to be a proper rate, had been in effect during the year ending June 30th, 1932, the earnings of Cities Service Gas Company would have been $5,777,110.00 or $1,310,641.00 less than a fair and reasonable return even if computed on the Commission's own rate base and on the Commission's own rate of return and replacement reserves, all of which conclusively shows said rate of 29½ cents is unjust, unreasonable, unlawful and confiscatory, all of which respondents will show if this application is allowed.

40

For the reason that said order of the Commission directing this respondent to reduce its rates is void and unenforceable because it is impossible for this respondent to [fol. 59] determine therefrom the amount of reduction so intended to be ordered.

41

For the reason that by making said order effective August 1st, 1932, and by directing this respondent to reduce its charges to its customers as of that date, respondent is placed in the position of guaranteeing the validity of said order and its final approval by the courts and in the event such order is, in the orderly course of such proceedings, determined to be invalid this respondent will have suffered the confiscation of its property during the entire period of litigation and will thereby suffer irreparable injury, respondent being informed and believing that the validity of said order will be contested in the courts.

42

For the reason that the finding of said Commission that there is a duplication in the services rendered by Henry L. Doherty & Company and by The Gas Service Company is without support in the evidence and is contrary to all of the evidence in regard thereto and is not true in fact.

43

For the reason that said Commission permitted to be introduced before it incompetent and irrelevant testimony and excluded from the evidence competent and relevant testimony offered by respondents and erroneously ruled upon

the several motions and objections made by the parties respectively during the course of said proceeding.

[fol. 60]

44

For the reason that said Commission, wholly without support in the evidence and in disregard of all evidence in relation thereto, eliminated from the valuation of the property of the Cities Service Gas Company as not used and useful the compressor stations at Hogshooter, Hominy and Owassa and refused to make any allowance whatever therefor.

45

For the reason that said Commission disregarded and ignored all evidence before it as to the going concern value of the Cities Service Gas Company, including the testimony of its own expert witness, and without any support whatever in the evidence arbitrarily reduced said item to an inadequate amount.

46

For the reason that said Commission arbitrarily and without any evidence in support thereof, eliminated the item claimed by respondents as cost of financing entering into the rate base of the Cities Service Gas Company.

47

For the reason that said Commission unlawfully and arbitrarily disregarded the evidence and misconstrued and misinterpreted the same as to all of the property accounts of the Cities Service Gas Company and all matters discussed in the original and reply briefs of the respondents and likewise with respect to the contracts between the several respondents and Henry L. Doherty & Company and for the reason that the findings of said Commission as to [fol. 61] the intangible items entering into the rate base of the Cities Service Gas Company are without support in the evidence and contrary to the evidence.

48

For the reason that said Commission in its said decision, opinion, findings and order exceeded its jurisdiction and undertook to determine strictly legal questions, jurisdiction

with respect to which is, by the Constitution of the State of Kansas, vested exclusively in the courts.

49

For the reason that in said decision, opinion, findings and order the several respondents are ordered to reduce their respective rates in an amount equal to ten cents per M. C. F. on gas sold by them for domestic purposes plus an amount equal to 1¾ per cent of their gross revenue, in which respect said decision, opinion, findings and order, and each of them, are beyond the jurisdiction of the Commission, impossible of performance and void for the following reasons:

A. Said reduction is required to include 1¾ per cent of gross revenue from the sale of industrial gas sold on special written contracts and at a price which returns to the respondents respectively said 1¾ per cent on said sales respectively, such industrial sales having nothing whatever to do with this investigation as to the reasonableness of the contract for the sale of domestic gas at the city gates and the inclusion in said reduction of 1¾ per cent of gross revenue from industrial sales in a reduction to domestic consumers is unreasonable, unlawful, unjust and void.

[fol. 62] B. The amount represented by 1¾ per cent of gross revenue is an amount impossible of determination in advance, varies monthly and is not a definite, fixed, or ever determinable amount to be taken into consideration in establishing a rate on August 1st, 1932, as directed.

C. The rates of the several respondents are of many kinds and types including the three-part rate of the Union Public Service Company in effect at Ottawa; the two-part rate of The Western Distributing Company in effect in some twenty small towns in the vicinity of Wichita; rates consisting of a service charge and a commodity charge such as the rates of Union Public Service Company at Paola, Osawatomie and other cities in that locality; and step or block rates such as are used by practically all respondents in some of the cities served by them; that even if the amount of the reduction so attempted to be ordered could be determined there is no direction in said order as to how such reduction should be applied to the rate in ques-

tion, that is, whether it should affect a service charge and if so to what extent; how it should be applied to a three or two part rate—whether to the service charge, the demand charge or the commodity charge or to all, and if to all, in what proportions; how it should be applied to a step or block rate whether in the first step or block, the second or some subsequent one or whether to all and if so in what proportion; for all of which reasons said decision, opinion, findings and order, and each of them, are meaningless, unreasonable, unlawful, not possible of performance and void.

D. Under the laws of Kansas an existing rate can be changed by the Commission only after a full and lawful hearing, the finding on proper evidence that existing rates are unreasonable, and the substitution of a definite rate by [fol. 63] the Commission for the rate so found to be unreasonable, none of which things were done herein.

E. Respondents have no statutory or other right to put in effect a rate not established or approved by the Commission and any rate it might attempt to put in effect under said order would neither be so established or approved.

F. For all, or a part of which, reasons it would be impossible for this respondent to comply with said order and the same is void.

50

For the reason that the reduction attempted to be ordered put in effect applies alike to all respondents, the same as if their present rates were based on gas at forty cents per M. C. F. at the city gate, whereas such is not the fact, instances of which are the rates of The Arkansas Valley Gas Company at Arkansas City, based on local gas at fifteen cents per M. C. F. at the city gate; the rates of The Hutchinson Gas Company at Hutchinson, based on local gas at twenty-five cents per M. C. F. at the city gate, the rates of Union Public Service Company, based on an average city gate rate of thirty cents per M. C. F. at Parsons, using both main line and local gas, and twenty cents per M. C. F. at Cherryvale, using all local gas; the rates of The Newton Gas Company at Newton, based on local gas at twenty-five cents per M. C. F., and the rates of The Western Distributing Company at El Dorado, based on

local gas at the city gate at twenty-five cents per M. C. F.; and the rates of the Pittsburg Gas Company in effect under an injunction of the District Court of Shawnee County prohibiting the interference of the Commission by the rate [fol. 64] attempted by this order or otherwise. For all of which reasons said order is unreasonable, unjust, discriminatory, unlawful and void and if intended to require an adjustment of rates on the basis of 29½ cents at the city gate would require an increase in rates in all cities where existing rates are based on a city gate rate of less than 29½ cents instead of a reduction; that the Commission must take judicial knowledge of the rates of this respondent, part of its official records, and of the applicability of said order in these several respects to it, separate and apart from all other respondents.

51

For the reason that in respect to the several matters called to the attention of the Commission in each and all of the foregoing paragraphs the action of the Commission deprives this respondent of its property without due process of law; denies it the equal protection of the laws; impairs the obligation of its contracts; undertakes to legislate with respect to interstate commerce and usurps the business management of the several companies involved, all in violation of the Constitution of the United States and the Constitution and laws of the State of Kansas and particularly Clause 3 of Section 8 of Article 1, the first subdivision of Section 10 of Article 1 of the Constitution of the United States and the Fourteenth Amendment thereto.

Wherefore, this respondent prays that said decision, opinion, findings and order be set aside and a rehearing granted it herein.

The Wichita Gas Company, by Robt. D. Garver, Robert Stone, Attorneys.

[fol. 65] EXHIBIT "E" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts, and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Wichita Gas Company, Wichita, Kansas;
Hutchinson Gas Company, Hutchinson, Kansas;
Newton Gas Company, Newton, Kansas;
Pittsburg Gas Company, Pittsburg, Kansas;
Capital Gas & Electric Company, Topeka, Kansas;
Wyandotte Gas Company, Kansas City, Kansas;
Arkansas Valley Gas Company, Arkansas City, Kansas;
Girard Gas Company, Girard, Kansas;
Union Public Service Company, 43 towns;
Western Distributing Company, 27 towns;
Winfield Natural Gas Company, Winfield, Kansas;
Tri-City Gas Company, Kansas City, Mo.;
Gas Service Company, Kansas City, Mo.;
American Pipe Line Company, Bartlesville, Okla.,
Respondents

Order Granting a Rehearing

Now, on this 5th day of August, 1932, the application of the respondents for a rehearing in the above entitled matter comes regularly before the Commission for final determination. The application contains fifty-one alleged grounds for a rehearing. After considering all of the allegations contained in the respondents' application, the Commission finds:

That all but one of the fifty-one grounds alleged by the [fol. 66] respondents in their application for a rehearing are without merit, and present no issues which were not fully considered by the Commission in the original proceedings.

That paragraph thirty-nine of respondents' application does present new matter and requires evidence which was not available at the time the original hearing before the

Commission was closed. That said paragraph thirty-nine of respondents' application for a rehearing goes to the decreased earnings of the Cities Service Gas Company for the year ending June 30, 1932, and should receive consideration by this Commission.

The Commission therefore further finds:

That a rehearing should be granted the respondents in the above entitled cause, and that the respondents should be given an opportunity to show the earnings of the Cities Service Gas Company for the year ending June 30, 1932.

The Commission further finds that the rehearing should be set for ten o'clock, on August 15, 1932, at the offices of the Commission, in the State House, Topeka, Kansas.

The Commission further finds that the order issued on the 30th day of July, 1932, in the above entitled matter, should be suspended pending final determination of the matter on rehearing.

It is therefore, by the Commission ordered, That the application of the respondents in the above entitled cause be, and the same is hereby granted; that a rehearing be held at ten o'clock on August 15, 1932, at the State House, Topeka, Kansas, at which time the respondents will be given an opportunity to present evidence in behalf of their allegation as to the earnings of the Cities Service Gas Company for the year ending June 30, 1932.

It is further by the Commission ordered that the order of this Commission issued on the 20th day of July, 1932, in [fol. 67] the above entitled matter, be, and the same is hereby, suspended, pending final disposition of the matter after the rehearing.

J. W. Greenleaf, Thurman Hill, Chas. W. Campbell.
Attest: Herman L. Gees, Secretary.

[fol. 68] EXHIBIT "F" TO BILL OF COMPLAINT

The Wichita Gas Company

This respondent offers to show by the witnesses F. C. Hamilton and Fred H. Rice that the present value of its property used and useful in rendering service to its consumers in the city of Wichita, Kansas, is $2,872,854.00.

That its gross earnings for the year ending June 30th, 1932, were $1,818,850.00.

That for the year ending June 30th, 1932, it paid for purchased gas to the Cities Service Gas Company, from which it receives its entire supply, the sum of $1,175,116.00 at the rate of 40c per M. C. F. for domestic gas, of which it purchased 2,415,298 M. C. F.

That its operation and maintenance expense, exclusive of purchased gas, for said year ending was $462,638.00.

That the net earnings applicable to depreciation and return for said period were $181,096.00.

That the reduction in salaries effective June 15th, 1932, will result in a saving in operating expenses of $24,338.00.

That the earnings of the company for said year ending had said reduction in salaries been in effect during the entire period would have been $205,434.00, which would be a return of only 7.2 per cent on the present fair value of its property.

That the net earnings for said period reflect profit from sales to the Kansas Gas & Electric Company for a five months' period in the amount of $18,669.00; that this customer is no longer connected and the net earnings should be reduced by this amount in order to represent a normal year and would leave the net earnings $186,765.00 or 6.5 per cent of the present fair value of the property.

That the County Assessor of Sedgwick County, the local Board of Equalization and the State Tax Commission have [fol. 69] increased taxes of The Wichita Gas Company $1,000,000.00 over the amount returned by the company, which will result in an increase of taxes in the amount of $31,298.00, which should be deducted from the above net earnings in order to represent the future normal year which would reduce the net earnings of the company to $155,467.00 or 5.4 per cent on the present value.

The company is unable to procure gas at the city gate for less than the price now being paid; that existing rates do not permit said company to make a fair return on the fair value of its property and that the reduction in rates attempted to be ordered in the Commission's order of July 20th is unreasonable, unjust and would result in the confiscation of its property.

[fol. 70] EXHIBIT "G" TO BILL OF COMPLAINT

Respondents offer to show by the witness A. W. Ambrose that he is Vice President and Assistant General Manager

of the Cities Service Gas Company; that he has been with said company since the year 1923; that prior thereto he was Chief Petroleum Technologist of the Bureau of Mines of the United States Government; that he is familiar with the gas reserves of Cities Service Gas Company, most of which were purchased under his direction and supervision; that in his opinion as an officer of said company they are all necessary in order to guarantee service to the consumers on said system; that the reserves of 71,267 acres allowed by the Commission are not adequate; that said 71,267 acres do not have the reserves of gas available to Cities Service Gas Company which the Commission found; that during 1931 the total volume of gas taken from the Texas panhandle field was 1,263,000,000 feet per day, of which only 219,000,000 feet per day was taken by pipe lines, or approximately 17 per cent; that the gas not delivered to pipe lines was used in gasoline plants, carbon black plants, the production of oils, or blown in the air and will continue to be so used or wasted in the same proportions unless prohibited by lawful orders of the Texas Commission; that said Commission now has under consideration an order limiting all takes from wells to five (5%) per cent of the open flow and an order shutting in all wells having unconnected offsets; that if the Texas Commission makes the proposed order and it is enforced the 71,257 acres allowed by this Commission will be wholly inadequate for even the coming winter, and if the Cities Service Gas Company restricts its takes to the acreage allowed by this Commission, [fol. 71] service will fail; that under present practices in Texas the owners of approximately ten (10%) per cent of the leases are producing approximately eighty-two (82%) per cent of the gas, none of which is connected to pipe lines or used by them; that such practices have reduced rock pressure in the Borger territory from the original 430 pounds to less than 50 pounds; that gas in the area, including the 71,267 acres allowed by this Commission is migrating to the low pressure Borger area; that the reserves of gas under said 71,267 acres are being thus constantly depleted and are not available to the Cities Service Gas Company as assumed by this Commission; that in its computa-

tion of proper reserves this Commission has included the open flow of wells transferred to Texoma, amounting to approximately 250,000,000 feet per day; that all of these matters are necessary to be taken into consideration in determining proper reserves and were not considered by this Commission as known by it; that the reserves of the Cities Service Gas Company are not in excess of proper reserves as recognized by the gas industry and as owned and held by other major pipe line companies; that none of the gas acreage now held by Cities Service Gas Company was bought or is being held for speculation.

EXHIBIT "H" TO BILL OF COMPLAINT

Respondents offer to show by the witness H. L. Eastman that dry hole allowance of $12,000.00 per year is wholly insufficient, unjust and unreasonable for the reason that in 1930 Cities Service Gas Company drilled ten (10) dry holes at a cost of $174,748.00 and in 1931 drilled two (2) dry holes at a cost of $126,339.00; and it is impracticable to undertake any exploratory drilling for $12,000.00.

[fol. 72] EXHIBIT "I" TO BILL OF COMPLAINT

Respondents offer to show by the witnesses Ed Warren, J. G. Dickinson and Ross M. Stumtz that they are each and all familiar with the cost of gas wells in the Texas panhandle territory; that the witness Ritchie, who testified for the Commission and whose testimony was adopted by it in its findings, never drilled a gas well in the Texas panhandle and was not familiar with such costs; that neither the Marland Oil Company or Continental Oil Company, successor to the Marland Oil Company, and with which the witness Ritchie was supposed to have attained his experience and knowledge, drilled gas wells in the fields concerning which Ritchie undertook to testify; that rotary drilling is not generally used in said fields for gas wells and that the cost of rotary wells is greater than the cost of wells drilled with standard tools.

EXHIBIT "J" TO BILL OF COMPLAINT

All Respondents

These respondents offer to show by the witnesses F. C. Hamilton and Fred H. Rice that the present value of their property used and useful in rendering service to their consumers in all of said cities is $15,326,298.00.

That their gross earnings for the year ending June 30th, 1932, were $7,092,398.00.

That for the year ending June 30th, 1932, they paid for purchased gas from all sources $4,517,230.00.

That their operation and maintenance expenses, exclusive of purchased gas, for said period were $1,909,935.00.

That the net earnings applicable to depreciation and re-
[fol. 73] turn for said period were $665,233.00 to be adjusted by the deductions shown in the offer for Wichita.

That had the present salary reductions been in effect for the entire period the operating expenses would have been reduced in the sum of $91,756.00 and the net earnings would have been increased to $756,989.00, or 4.9 per cent on the fair value of all properties.

[fol. 74] EXHIBIT "K" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Part A. Wichita Gas Company, Wichita, Kansas.
B. Hutchinson Gas Company, Hutchinson, Kans.
C. Newton Gas Company, Newton, Kansas.
D. Pittsburg Gas Company, Pittsburg, Kans.
E. Capital Gas and Electric Company, Topeka, Kans.
F. Wyandotte Gas Company, Kansas City, Kansas.
G. Arkansas Valley Gas Company, Arkansas City, Kans.

H. Girard Gas Company, Girard, Kansas.
I. Union Public Service Company, 45 towns.
J. Western Distributing Company, 27 towns.
K. Winfield Natural Gas Company, Winfield, Kans.
L. Tri-City Gas Company, Kansas City, Mo.
M. Gas Service Company, Kansas City, Mo.
N. American Pipe Line Company, Bartlesville, Okla.

Opinion on Rehearing

The above investigation of the reasonableness of the contracts and charges made by holding companies to subsidiary companies of the Cities Service Company doing business in the State of Kansas, comes now before the Commission for final decision on rehearing.

[fol. 75] On the 20th day of July, 1932, the Commission issued an order in the above entitled matter in which it found that the payments made by the respondent companies to Henry L. Doherty & Company in the amount of one and three-fourths per cent of the gross revenues of the distributing companies were unreasonable and excessive; that 29.5 cents was the reasonable price to be paid to the Cities Service Gas Company by the respondents for main line town border gas, and that any amount paid in excess thereof was unreasonable.

The respondent companies filed an application for rehearing setting up fifty-one separate grounds therefor. After due consideration the Commission found that the only new matter presented in the application for rehearing was that set out in paragraph 39 of the application for rehearing, which claimed a decrease in the earnings of the Cities Service Gas Company for the year ending June 30, 1932.

On the 5th day of August, 1932, the Commission granted the application of respondents for rehearing in order to give the respondents an opportunity to show earnings of the Cities Service Gas Company for the year ending June 30, 1932. The rehearing was held on the 15th day of August, 1932, at which time respondents introduced evidence and an earning statement as to the earnings of the Cities Service Gas Company for the year ending June 30, 1932. The company also asked for permission to introduce evidence to show that compressor

station spare parts had not been included in the inventories; that the Commission had made an error of $5,000,000 in calculating the annual depreciation requirements of the company; and that the Commission had included in its calculation of gas available for the use of the Cities Service Gas Company nine wells which had been [fol. 76] sold to the Texhoma Gas Company. These three items will be discussed in advance of the earnings for the year ending June 30, 1932.

Compressor Station Spare Parts

While it appears that the company keeps strict accounting of its materials and supplies on hand in various warehouses located at points generally over the system, it failed to include in its books and accounts which purport to show the cost of materials and supplies on hand currently, some replacement or repair parts in compressor stations of the value of $119,275.

The testimony shows that these replacement and repair parts were present at compressor stations on September 1, 1931, and were not included in the book value of materials and supplies on hand at that date.

The Commission, therefore, finds that the fair value of the pipe line system at September 1, 1931, should be increased from $73,029,235 to $73,148,510 to take into account this material.

Annual Depreciation and Replacement Reserves

The respondents introduced evidence on the rehearing to the effect that the Commission in calculating the annual depreciation and replacement reserve requirements had made an error of $5,000. In its original opinion, on page 132 of the typewritten copy, the Commission accepted the per cent allowances as claimed by the respondents and applied them to the present cost of reproduction as found by the Commission. By applying these percentages to the values which the Commission found, it calculated that the annual allowances for physical property would be $1,894,022, based on physical property values of [fol. 77] September 1, 1931. This was the figure used by the Commission in its calculation. The figure of $1,889,022

found on page 132 was a typographical error and not used by the Commission in its calculation. The proper result was, therefore, reached and the typographical error requires no adjustments in the Commission's final conclusions.

Gas Reserves

Respondents contend that the Commission in its computation of probable reserves, has included the open flow of wells transferred to the Texhoma-Company amounting to 250,000,000 feet per day. On page 449 of the Transcript, Mr. Nesbit, the company's chief geologist, testified that the sixty wells owned by the company had an open flow of approximately one billion and a half cubic feet of gas per day. "The latest report I have happened to have a note on here, a billion five hundred thirty-two million six hundred twenty-five thousand.

Q. Sixty wells, I take it, that is there are sixty wells?
A. Yes, sir; we have sixty wells.
Q. This open flow was for sixty wells?
A. Yes, sir; I think that is correct" (Tr. 449).

It appears quite evident, therefore, that the amount of open flow used by the Commission in determining the gas available to the company was from the sixty wells owned by the company. If the open flow in that particular field were further reduced to 250,000,000 cubic feet per day the calculation of the Commission would not be materially affected.

[fol. 78] Earnings for Year Ending June 30, 1932

During the rehearing in this case respondents introduced Exhibit 102, purporting to show the financial results of the operations of the pipeline system during the year ended June 30, 1932, in support of its contention that due to depressed economic conditions its earnings had decreased since this investigation was started and that it was no longer enjoying the prosperity of former years.

Page 1 of Exhibit 102 purports to show the net income during the year ending June 30, 1932, amounted to $7,861,516.85.

Included in expenses in arriving at this net income is an item of $52,297.13 representing payments to Henry L.

Doherty & Company under the 1¾ per cent contract and $50,000 rate case expenses. Deducting from expenses the payments to Henry L. Doherty & Company, for reasons elsewhere stated herein, and deducting the item of rate case expenses, because it is an abnormal nonrecurring item, results in net income before allowance for depreciation and depletion of $7,963,813.

After allowances are made for depreciation, depletion, amortization and dry hole expenses, aggregating $1,977,591, being the aggregate of such allowances found by the Commission based on September 1, 1931, value, results in a net income of $5,986,222.

The net income of $5,986,222 is equal to more than 8 per cent of the fair value of the pipeline system property at September 1, 1931, as found by this Commission, of $73,149,510.

The average net income during the year ended December 31, 1930, and the twelve months ended June 30, 1931, as heretofore found by this Commission, added to the net in- [fol. 79] come for the twelve-month period ended June 30, 1932, of $5,986,222 results in an average net income during these three annual periods of $6,769,936 which is equal to 9.87 per cent of the average value during these periods and 9.25 per cent of the value at September 1, 1931, of $73,148,510.

The net income before depreciation and depletion for the three annual periods were as follows:

December 31, 1930	$9,006,687
June 30, 1931	8,889,565
June 30, 1932	7,963,813

giving an average annual income over the three periods of $8,620,022.

The depreciation and depletion requirements for the three annual periods under investigation were as follows:

December 31, 1930	$1,776,881
June 30, 1931	1,795,785
June 30, 1932	1,977,591

Which results in an average annual depreciation and depletion requirement of $1,850,086, which subtracted from the average annual income before depreciation and depletion

gives us an average net income available for return on investment of $6,769,936.

The average town border main line gas sales during the three periods under investigation amounted to 20,560,450 M. C. F., which produces an average annual revenue of $8,138,523.

If this main line domestic gas were sold at thirty cents per M. C. F. it would have produced a revenue of $6,168,135, which would have resulted in a reduction in revenue of $1,970,388, this assuming that the 30-cent rate applied over the entire system—in fact it applies only to Kansas and therefore reductions in revenues would be much less [fol. 80] than $1,970,388; however, using the figures of $1,970,388, the net income available for return on investment would be $4,799,548. The average fair values during the three periods covered by the investigation were as follows:

Twelve Months ending Dec. 31, 1930	$66,296,147
June 30, 1931	66,912,061
June 30, 1932	73,148,510

Which results in an average value over the three periods of $68,785,573. The average net income during the periods covered by the investigation would have produced a rate of return of 7 per cent which the Commission has found reasonable in this investigation. The effect of the economies of the company put into practice since the investigation commenced by reducing administration expenses and paying less for gas should result in the company returning more than 7 per cent on the valuation fixed by the Commission.

In arriving at the determination as to what return may be expected, the Commission now has available the three annual periods. It is the belief of the Commission that a more accurate result is arrived at by considering the three annual periods than if the investigation had covered but one year. Consideration must also be given to the fact that the three years covered by the investigation have been years of economic depression and periods when the earnings of the company have been unusually low. The advantage of adopting a number of years as a test period was well expressed by Judge McDermott in the recent case of Denver Union Stock Yards Company v. United States, 57 F. (2d) 735, 752, in which he said:

"In arriving at a determination of what return may be expected of rates that are promulgated for the future, it is [fol. 81] proper to look to the experience of the past as a guide. For that reason, in all rate hearings, a test period is selected and a study made of the revenue and disbursements for that period. Ordinarily a test period of five years or more, if available, is selected. What the test period shall be depends on circumstances; for example, the years of the war are ordinarily excluded for the reason that such years are abnormal. Laying to one side such abnormalities, it is generally true that, the longer the test period, the more accurate the judgment for the future; the broader the base, the safer the estimate. When there has been a reasonably steady growth in the business, and reason to anticipate that it will continue, the factor of growth should be considered in estimating the future."

The Commission finds that consideration should be given to the decreased earnings and has made such adjustment by averaging the period in which the decreased earnings occurred with the other two annual periods under investigation.

The testimony during the rehearing of witnesses appearing for the respondents was to the effect that various operating economies had been inaugurated at about the close of the twelve months ending June 30, 1932, which will result in material reductions in expenses. The saving by reductions in wages and salaries alone will amount to approximately $104,000 per year, but this saving is reflected in the net income for the year ended June 30, 1932, for a period of only two weeks, the reduction having been effective beginning June 15, 1932.

For the purpose of comparing the net income of June 30, 1932, with a figure representing fair value, the Commission has used the fair values as heretofore found and has not given effect to any reductions which might be re- [fol. 82] quired in such values due to lowering of material and labor prices since the time of the valuation.

The financial position of the company at June 30, 1932, indicates that this system is enjoying a marked degree of prosperity in the face of generally otherwise depressed conditions. It reduced its indebtedness to its parent company from $9,000,000 at June 30, 1931, to $6,500,000 at June

30, 1932; it increased its replacement reserve from $10,818,020 at June 30, 1931; to $12,455,838 at June 30, 1932, even after absorbing deferred charges to the reserve, which have been carried as deferred charges on the balance sheet, to the extent of approximately $750,000. The company has a surplus of $7,852,103.40; it has reduced its current liabilities at June 30, 1932, compared with June 30, 1931, and was able to loan to affiliated companies and have owing it at June 30, 1932, from such affiliated companies $2,911,654.13.

A large part of the decreased earnings during the past year has been caused by loss of sales of industrial gas. This has decreased the earnings of the Cities Service Company in approximately $1,000,000. It is only reasonable to assume that industries will soon continue operation and that the loss of industrial sales will be only a temporary abnormal condition.

Evidence introduced at the rehearing disclosed that the respondents have reduced rates at the city gate and to the consumers in several cities in Kansas.

The domestic consumer should not be required to carry all of the loss in revenue from the industrial gas, but the company which has enjoyed prosperous years in the past should be willing to absorb a part of this loss during the abnormal time. The Commission is of the opinion that most of the gas pipeline companies, situated as is the Cities Service Gas Company, would be satisfied with a return, [fol. 83] under present conditions, of much less than 7 per cent. The Commission, therefore finds that 30 cents is a reasonable price to be paid by the respondent distributing companies purchasing main line town border domestic gas from the Cities Service Gas Company, and that anything charged in excess thereof by the pipeline company to the distributing plants is unreasonable.

The Commission further finds that under authority of Chapter 204 of the Laws of 1931, the costs of this proceeding in the sum of $66,936.08 should be taxed against the respondents.

An appropriate order will be issued in accordance with the findings in the original opinion as modified by this supplemental opinion on rehearing.

Thurman Hill, Chas. W. Campbell, Commissioners.

Attest: Herman L. Gees, Secretary.

Chairman Greenleaf dissenting in part.

After full consideration of all the facts in the case, including all the evidence submitted in the rehearing held in the Commission hearing room August 15, I am still convinced that the reasonable price to be paid for main line town border domestic gas to the pipeline company, by its affiliated distributing company at the city gate is 32 cents per 1000 cu. ft., and any amount above that price is unreasonable.

Jesse W. Greenleaf.

[fol. 84] EXHIBIT "L" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Part A. Wichita Gas Company, Wichita, Kansas;
B. Hutchinson Gas Company, Hutchinson, Kansas;
C. Newton Gas Company, Newton, Kansas;
D. Pittsburg Gas Company, Pittsburg, Kansas;
E. Capital Gas and Electric Company, Topeka, Kansas;
F. Wyandotte Gas Company, Kansas City, Kansas;
G. Arkansas Valley Gas Company, Arkansas City, Kansas;
H. Girard Gas Company, Girard, Kansas;
I. Union Public Service Company, 45 towns;
J. Western Distributing Company, 27 Towns;
K. Winfield Natural Gas Company, Winfield, Kansas;
L. Tri-City Gas Company, Kansas City, Mo.;
M. Gas Service Company, Kansas City, Mo.;
N. American Pipe Line Company, Bartlesville, Okla.,
Respondents

Order

Now, on this 31st day of August, 1932, the above matter comes regularly before the Commission for final determina-

tion upon the application of respondents for a rehearing, which was limited by the Commission to ground thirty-nine in the motion of respondents, and the Commission finds:

[fol. 85] 1

That during the year ending June 30, 1932, there was a falling off of sales of respondents' domestic gas in the sum of approximately $400,000, as compared with the year ending June 30, 1931.

2

That certain economies put into effect by the respondents since June 1, 1932, will result in an annual savings of $104,000.

3

That since June 1, 1932, respondents are buying and attempting to buy field gas at 6 cents instead of 8 cents per M. C. F., and that this policy will also reduce operating expenses.

4

That with these savings deducted from the net earnings, the reduction in earnings for the next fiscal period should not be in excess of $300,000.

5

That it would be inequitable to accept this figure of reduction in earnings without taking into consideration that reproduction costs new at this time would also cut valuations fixed by the Commission in its original opinion substantially.

6

That the findings in the opinion in the above entitled matter signed on the 19th day of July, 1932, as supplemented by the opinion on rehearing, should be and hereby are incorporated in this order and made a part hereof.

[fol. 86] 7

The distributing companies, respondents above named, and the Cities Service Gas Company, are mere agents or instrumentalities of the Cities Service Company.

8

That the contract between Henry L. Doherty & Company and the various distributing companies, respondents above named, under which Henry L. Doherty & Company purports to render various departmental services to the distributing companies, and receives as consideration therefor one and three-fourths per cent of the gross revenues of the distributing companies; an engineering fee of five per cent of the cost of construction; a fee for services of the securities department and an additional expense and per diem charge is unreasonable, and that the compensation received thereunder is excessive to the extent of the payment of the one and three-fourths per cent of the gross revenues of the distributing companies.

9

That the contract between the Cities Service Gas Company, a natural gas pipe line company, and respondents above named, under which the Cities Service Gas Company sells gas to the distributing companies at the city gate at an average price of 39.5 cents per M. C. F. is unreasonable, and that the payments made thereunder are excessive above the amount of 30 cents per M. C. F. for such main line border gas.

[fol. 87]

10

That 30 cents is a reasonable price to be paid to the Cities Service Gas Company by the respondents for main line town border gas, and that any amount paid in excess thereof is unreasonable.

11

That the costs hereof incurred by the Commission herein, amounting to $66,936.08, should be taxed to and paid by the respondents.

12

That on and after the 1st day of September, 1932, the distributing companies, respondents above named, shall cease to set up on their books as an expense item any payments made to Henry L. Doherty & Company under the contract above mentioned, because of the one and three-fourths per cent charge and also any payment made to Cities Service Gas Company for main line town border gas in excess

of 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

It is therefore by the Commission ordered:

1

That on and after the 1st day of September, 1932, the distributing companies, respondents above named, shall cease to set up on their books as an expense item any payments made to Henry L. Doherty & Company under the contract above mentioned, because of the one and three-fourths per cent charge and also any payments made to Cities Service Gas Company for main line town border gas in excess of [fol. 88] 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

2

That on the 17th day of October, 1932, the distributing companies, respondents above named, appear before the Public Service Commission, at 10:00 o'clock A. M., and show cause to the Commission why the reduction in expenses as above set forth should not be passed on to the consumers with such other reductions as may be found reasonable.

Thurman Hill, Chas. W. Campbell. Attest: Herman L. Gees, Secretary.

[fol. 89] EXHIBIT "M" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

Docket No. 13127

In the matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company.

Part A. Wichita Gas Company, Wichita, Kansas;
B. Hutchinson Gas Company, Hutchinson, Kansas;
C. Newton Gas Company, Newton, Kansas;

D. Pittsburg Gas Company, Pittsburg, Kansas;
E. Capital Gas and Electric Company, Topeka, Kansas;
F. Wyandotte Gas Company, Kansas City, Kansas;
G. Arkansas Valley Gas Company, Arkansas City, Kansas;
H. Girard Gas Company, Girard, Kansas;
I. Union Public Service Company, 45 Towns;
J. Western Distributing Company, 27 Towns;
K. Winfield Natural Gas Company, Winfield, Kansas;
L. Tri-City Gas Company, Kansas City, Mo.;
M. Gas Service Company, Kansas City, Mo.;
N. American Pipe Line Company, Bartlesville, Okla.,
Respondents

Order

Now, on this 31st day of August, 1932, the Commission having found that 30 cents per M. C. F. is a reasonable price for the respondents above named to pay the Cities Service Gas Company for main line town border domestic gas, and that anything in excess thereof is unreasonable, [fol. 90] the Commission now has before it for consideration the question of determining the manner in which this reduction in expenses should be passed on to the consumer.

The Commission, therefore, finds that effective September 1, 1932, and until a hearing is held and an order issued, that the distributing companies, respondents above named, should charge rates to the consumers as follows:

All distributing companies paying a gate rate in excess of 30 cents per M. C. F. shall deduct the difference between what the distributing company is now paying at the city gate and 30 cents per M. C. F. and pass on this difference to the consumer.

It is therefore by the Commission ordered, that effective September 1, 1932, and until a hearing is held and an order issued, that the distributing companies, respondents above named, shall charge rates to the consumers as follows:

All distributing companies paying a gate rate in excess of 30 cents per M. C. F. shall deduct the difference between what the distributing company is now paying at the city

gate and 30 cents per M. C. F. and pass on this difference to the consumer.

By the Commission it is so ordered.

Thurman Hill, Chas. W. Campbell, Commissioners.

Attest: Herman L. Gees, Secretary.

[fol. 91] EXHIBIT "N" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by holding Companies to Subsidiary Companies of the Cities Service Company

Application of The Wichita Gas Company for Rehearing on Opinion and Orders of August 31, 1932

Comes now The Wichita Gas Company, one of the parties to the above proceeding, and fully reserving all its rights, as set out in its special appearance filed herein at the inception of this matter, applies for a rehearing in respect to all matters found and ordered and purported to have been determined here in by this Commission in its opinion and orders of August 31st, 1932, for the reason that said opinion, findings and orders, severally and collectively, are unlawful, unjust and unreasonable in the following respects and for the following reasons:

1

For all of the reasons set out in respondent's application for a rehearing on the opinion, decision, findings and order of this Commission of July 20, 1932, heretofore filed herein and granted by said Commission as to paragraph 39 only, all of the allegations of said original application for rehearing being again urged as against said opinions and [fol. 92] orders of August 31st, 1932, except the allegations of paragraph 39 thereof.

2

For the reason that in its ruling and decision on respondent's original application for a rehearing this Commission

wrongfully, unlawfully, unreasonably and unjustly granted said application as to paragraph 39 only and on the subsequent rehearing refused to permit respondent to introduce evidence with respect to all other matters alleged in said application.

3

For the reason that in its opinion, findings and orders of August 31st, 1932, on rehearing said Commission neglected and refused to find the value of the property of the Cities Service Gas Company used and useful in rendering the service in which it is engaged as of the time of said rehearing, and neglected and refused to determine the earnings of said company as of said time and unjustly, unlawfully and unreasonably undertook to determine the reasonableness of its contract with respondent for respondent's supply of gas at the city gate on the basis of a valuation and earnings averaged over a period of years notwithstanding the fact that the earnings of said Cities Service Gas Company for the year ending June 30th, 1932, as shown by respondent's evidence on rehearing, represented earnings on all of the property of said Cities Service Gas Company, there being no material additions or extensions to said system during said period the earnings upon which were not included in the earnings as shown to said Commission.

[fol. 93]

4

For the reason that the two orders issued by said Commission on August 31st, 1932, are inconsistent and in direct conflict with the other, said Commission in one order having directed respondent to appear before it on October 17th, 1932, to show cause why a reduction in its operating expenses should not be passed on to its consumers, and in the other having ordered a reduction in rates as of September 1st, 1932, the day after said order was issued, one of said orders by its terms putting in effect an immediate reduction of rates of respondent and the other order by its terms postponing any reduction in rates until after the reasonableness and justice of such reduction should be determined by said Commission after affording respondent an opportunity to be heard.

5

For the reason that in said opinion and orders of August 31st, 1932, said Commission increased the rate of 29½ cents per M. C. F. to be charged by the Cities Service Gas Company, as found in its opinion, findings and order of July 20th, 1932, only one-half cent per M. C. F., notwithstanding the fact that in its said opinion, findings and orders of August 31st, 1932, it found the earnings of the Cities Service Gas Company for the year ending June 30th, 1932, to have fallen off $1,000,000.00 on account of decreased industrial business and $400,000.00 on account of a decrease in domestic business, or a total of $1,400,000.00, and said increase of one-half cent per M. C. F. is entirely inadequate to compensate for said decreased earnings.

[fol. 94]

6

For the reason that in said opinion, findings and orders of August 31st, 1932, said Commission eliminated from the operating expenses of the Cities Service Gas Company an item of $52,297.13 representing payments to Henry L. Doherty & Company under a contract between it and said Cities Service Gas Company, said Commission having no jurisdiction over said Cities Service Gas Company or Henry L. Doherty & Company for said purpose.

7

For the reason that said Commission in its opinion and orders of August 31st, 1932, eliminated from the operating expenses of Cities Service Gas Company an item of $50,000.00 covering rate case expenses, said item being a proper item of operating expense to be included therein.

8

For the reason that said Commission in its opinion and orders of August 31st, 1932, did not increase the replacement reserves of the Cities Service Gas Company as previously allowed to correspond with the increased valuation found for its property.

9

For the reason that said Commission in its opinion and orders of August 31st, 1932, after finding that the earnings

of the Cities Service Gas Company had decreased $1,400,000.00 from the previous year, arbitrarily and capriciously found without any support in the evidence that such de-
[fol. 95] crease for the year ending June 30th, 1932, would be only $300,000.00.

10

For the reason that said Commission in said opinion and orders assumed that the value of the property of the Cities Service Gas Company at the time of said rehearing would be less than the value found by said Commission in its original opinion, findings and order without any evidence in support thereof.

11

For the reason that said Commission in said opinion and orders of August 31st, 1932, prohibited this respondent from setting up on its books any sums payable to Henry L. Doherty & Company under respondent's contract with it or to Cities Service Gas Company under its contract with it for purchased gas in excess of the price of 30 cents per M. C. F., said Commission being without authority to dictate the manner in which respondent's books should be kept.

12

For the reason that said Commission in its conduct of said proceeding has exceeded its jurisdiction and proceeded in direct violation of the limitations placed upon its jurisdiction by Chapter 239 of the Session Laws of 1931, wherein its jurisdiction is expressly limited to the determination of issues arising in a case the purpose of which is to "ascertain the reasonableness of a rate or charge to be made by a public utility."

[fol. 96] 13

For the reason that in its order of July 2nd, 1931, instituting Docket Number 13127 said Commission limited its investigation to the reasonableness of contracts made with and services rendered to subsidiary companies of the Cities Service Company by their various holding companies, said order expressly eliminating from the issues presented by said order the reasonableness of any contracts between subsidiary companies.

Wherefore this respondent prays that said opinion, findings and orders of August 31st, 1932, be set aside and a rehearing granted it herein.

The Wichita Gas Company, by Robt. D. Garver, Robert Stone, Attorneys.

[fol. 97] EXHIBIT "O" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Supplemental Application of the Wichita Gas Company for Rehearing on Opinion and Orders of August 31, 1932

Comes now The Wichita Gas Company, one of the parties to the above proceeding, and fully reserving all its rights, as set out in its special appearance filed herein at the inception of this matter, files this supplement to its application for rehearing on the said opinion and orders of August 31, 1932, hereby calling to the attention of said Commission matters transpiring subsequent to the time said application for rehearing was filed herein.

In addition to all matters set out in former applications for rehearing filed herein, respondent alleges that on the 9th day of September, 1932, the duly constituted, regulatory body of the State of Texas issued an order, a copy of which is not yet available to respondent and cannot be hereto attached, but in which order said Commission restricted the takes of all wells to not more than four per cent (4%) of the potential capacity of such well or wells, or so much of such potential capacity as may be necessary to take care of current demands for domestic and industrial use, said order thereby making it impossible for the Cities [fol. 98] Service Gas Company to take from any wells drilled subsequent to the promulgation of said order in excess of four per cent (4%) of the potential capacity of such wells by reason of which all calculations of this Commission in its original opinion finding proper gas reservations

for said Cities Service Gas Company become erroneous and not applicable, and said allowed reserves become entirely inadequate, the same being based on the ability of said Cities Service Gas Company to take from all wells drilled on its allowed acreage twenty per cent (20%) of the open flow thereof.

For the further reason that the limitation and restriction so placed by the State of Texas on gas wells in said state makes necessary and essential to service all of the reservations owned by said Cities Service Gas Company and disallowed by this Commission.

Wherefore, respondent prays for a rehearing in accordance with its application filed herein.

Robert D. Garver, Robert Stone, Attorneys for said Company.

[File endorsement omitted.]

2

[fol. 99] EXHIBIT "C" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company, viz:

Wichita Gas Company, Wichita, Kan.;
Hutchinson Gas Company, Hutchinson, Kan.;
Newton Gas Company, Newton, Kan.;
Pittsburg Gas Company, Pittsburg, Kan.;
Capital Gas and Electric Company, Topeka, Kan.;
Wyandotte Gas Company, Kansas City, Kan.;
Arkansas Valley Gas Company, Arkansas City, Kan.;
Girard Gas Company, Girard, Kan.;
Union Public Service Company, 45 Towns;
Western Distributing Company, 27 Towns;
Winfield Natural Gas Company, Winfield, Kan.;
Tri-City Gas Company, Kansas City, Mo.;

Gas Service Company, Kansas City, Mo.;
American Pipe Line Company, Bartlesville, Okla.;
Respondents

Opinion by the Commission

The above investigation of the reasonableness of the contracts and charges made by holding companies to subsidiary companies of the Cities Service Company doing business in the state of Kansas comes now before the Commission for final decision.

Upon the 2d day of July, 1931, the Commission on its own motion ordered an investigation of such contracts and charges, and set down said matter for hearing upon the 18th day of August, 1931. Owing to the magnitude of the task and in order that the parties be given fair opportunity to present their evidence, the case was continued from time to time and the first evidence was submitted on October 16, [fol. 100] 1931. The hearing was closed February 16, 1932. During this time the Commission heard testimony for twenty-six full days and received 101 exhibits, some of the exhibits containing several thousand pages. This evidence was introduced by forty witnesses, and the evidence when finally transcribed consisted of 2,901 pages of testimony. After the completion of the case the Commission granted the respondents and counsel for the state time to prepare and submit original and reply briefs, and these briefs have been submitted to and considered by the Commission.

Three contracts are involved in the investigation:

1. The contract between the Gas Service Company and the various distributing companies, respondents above named, under which the Gas Service Company operates and manages the distributing companies and keeps some of their books, and charges to such distributing companies certain sums monthly, purporting to be each distributing company's share of the expenses of the Gas Service Company.

2. The contract between Henry L. Doherty and Company and the various distributing companies, respondents above named, under which Henry L. Doherty and Company purports to render various departmental services to the distributing companies and receives as compensation therefor 1¾ per cent of the gross revenues of the distributing companies, an engineering fee of 5 per cent of the cost of con-

struction, a fee for services of the securities department, and an additional expense and per diem charge.

3. The contract between the Cities Service Gas Company, a natural gas pipe-line company, and the various distributing companies, respondents above named, under which the Cities Service Gas Company sells natural gas to the distributing companies at the city gates for 40 cents per M c. f., and in some cases less. This is a day-to-day contract, and is not in writing.

The American Pipe Line Company and the Cities Service Gas Pipe Line Company are also natural gas pipe line companies, included in the investigation. They are owned and controlled by the Cities Service Company. The property of the Cities Service Gas Pipe Line Company is leased, managed and operated by the Cities Service Gas Company, and its property is included in this investigation as the property of the latter company. The American Pipe Line Company being a unit of the pipe-line system, its earnings, expenses and property are consolidated with that of the [fol. 101] Cities Service Gas Company. The pipe-line companies will, therefore, be referred to in this opinion as the Cities Service Gas Company.

In order to get a clear picture of the reasons actuating the Commission in making the order of investigation it might not be amiss to relate a short history of the development of the gas resources of the state of Kansas, and its consequent effect on the consumers. It has been more than fifty years since gas was first produced in Kansas. At that time the commercial possibilities of gas in Kansas was given little consideration because of the limited market. The first use made of the gas from the first well in Kansas was to illuminate, through the use of flambeau lights, a country dance platform in Miami county, Kansas. As further gas wells were discovered the commercial possibilities were realized; companies were formed to drill gas wells and distribute gas to the people of Kansas.

During the past thirty years various fields have been discovered throughout the state and have been developed by producing and pipe-line companies. During this period of time much was learned by the gas industry as to methods of producing gas, and also in distributing the product to the consumer. One of the pioneers producing and distributing gas in this state was the Kansas Natural Gas

Company. Its history was rather a turbulent one, and finally, after receivership, its properties passed into the hands of the Cities Service Company.

This pioneer company served a very useful purpose. Its history taught other gas companies the value of conservation methods in the production of gas, and that by improvement in pipe-line methods much waste could be prevented at savings both to the company and the consumer. These matters were thoroughly developed in 1923 and 1924, when the Commission of Kansas was called upon to fix a fair and reasonable gate rate for the Kansas Natural Gas Company which was then owned and controlled by the Cities Service Company. At that time it was disclosed that one of the reasons for the forty-cent rate was the loss sustained from leakage. It was disclosed that the company lost a substantial part of the gas through this type of waste from the time the gas left the well until it reached the burner tip. It was further shown that the gas reserves at that time were problematical, most of the gas coming from shallow fields whose life expectancy was short and uncertain, creating a limited supply. This limited supply caused this company and other like companies to obtain large sums of money for the purpose of trying to find other sources of gas reserves to supply its consumers. These items just [fol. 102] related were factors which undoubtedly moved the Commission to approve the forty-cent rate as a proper charge paid by distribtuing companies to the main pipeline companies.

Since the last investigation of pipe-line rates in 1923 by this Commission, there has been a most radical change in the natural-gas industry. At that time most of the gas supply was used locally. Enormous gas reserves have since been developed and pipe-line construction practices have been advanced, so that it is possible without appreciable waste to transmit gas over long distances. The conditions then existing which in order to conserve the gas supply required the restriction of sale of gas to domestic consumers, principally for cooking purposes, no longer exists.

The general trend of all prices since 1923 has been downward, in fact the existing level of prices in a number of instances is lower than at any time in the past fifty years.

The Commission recognized these changing conditions and believed that such change required a redetermination of the reasonableness of the forty-cent gate rate.

Jurisdiction

The Commission took jurisdiction of the investigation on the theory that services rendered and gas furnished by holding or affiliated companies were proper matters for consideration by the Commission in considering the reasonableness of rates of subsidiary or affiliated distributing companies, and that the reasonableness of the contracts, under which the holding or affiliated companies render service and furnish gas to the affiliated or subsidiary companies, is properly measured by the cost of service rendered and the cost of furnishing the gas.

The Commission finds from the undisputed evidence of the respondents that for all practical purposes Henry L. Doherty, doing business as Henry L. Doherty and Company, controls the voting power of the Cities Service Company.

The evidence also clearly discloses that all of the fiscal agency contracts under which Henry L. Doherty and Company is paid 1¾ per cent are made between Henry L. Doherty and Company on the one part and the directors of the subsidiary companies on the other part; that the common stock of the subsidiary or distributing companies is held by the Cities Service Company and that Henry L. Doherty and Company, having control of the Cities Service Company, has control of the election of the officers and directors of the subsidiary companies with which he contracts (Tr. 1679).

[fol. 103] Henry L. Doherty, individual, appoints the general auditor of Henry L. Doherty and Company. "With the general auditor, the directing head of these activities, rests the appointment or removal of secretaries and others in responsible positions in the office of all the Cities Service subsidiaries." (Ex. 11, p. 6.)

The common stock of the following distributing companies, respondents herein, is owned by the Gas Service Company with the exception of the directors' shares: Arkansas Valley Gas Company, Capital Gas & Electric Company, Girard Gas Company, Hutchinson Gas Company, Newton Gas Company, Union Public Service Company, Pittsburg Gas Company, Western Distributing Company, Wichita Gas Company, and Wyandotte County Gas Company. (Ex. 28.)

All of the common stock of the Gas Service Company, except qualifying directors' shares, is owned by the Cities

Service Company. Therefore, all of the common stock, with the exception of directors' shares of all the distributing companies, respondents herein, is owned and controlled by the Cities Service Company through its control and ownership of the Gas Service Company.

The common stock of the Cities Service Gas Company, which sells gas at the city gates to distributing companies now under investigation, with the exception of the directors' shares, is owned by the Empire Gas & Fuel Company. (Ex. 28.) All of the capital stock, with the exception of the directors' shares, of the Empire Gas & Fuel Company is owned by the Cities Service Company.

All of the stock of the Cities Service Gas Pipe Line Company and the American Pipe Line Company, except qualifying directors' shares, is owned by the Cities Service Company. (Ex. 28.)

It is, therefore, apparent that the common stock of all the distributing companies and all the gas pipe-line companies which sell them gas is through intercorporate relations owned and controlled by the Cities Service Company, and the voting power of the Cities Service Company is in turn controlled by Henry L. Doherty and Company.

The relationship of the companies are such that the same principles will apply to all companies involved in the three contracts under investigation and they need not be treated separately.

At the time this hearing began there was some dispute as to the right of the Commission to inquire into the reasonableness of these contracts. The case of the Western Distributing Company v. The Public Service Commission was [fol. 104] then before the United States supreme court for decision. There was a controversy between counsel for the gas companies and counsel for the Commission as to whether or not the authority of the Public Service Commission to make such investigation had been definitely established by the United States supreme court in the case of Smith v. Illinois Bell Telephone Company. (282 U. S. 133.)

The Western Distributing Company case has now been decided by the United States supreme court and this question has been definitely determined. In that case the court said:

"Having in mind the affiliation of buyer and seller and the unity of control thus engendered, we think the position of the appellees is sound, and that the court below was right in holding that, if appellant desired an increase of rates, it was bound to offer satisfactory evidence with respect to all the costs which entered into the ascertainment of a reasonable rate. Those in control of the situation have combined the interstate carriage of the commodity with its local distribution in what is in practical effect one organization. There is an absence of arms' length bargaining between the two corporate entities involved, and of all the elements which ordinarily go to fix market value. The opportunity exists for one member of the combination to charge the other an unreasonable rate for the gas furnished, and thus to make such unfair charge in part the basis of the retail rate. The state authority whose powers are invoked to fix a reasonable rate is certainly entitled to be informed whether advantage has been taken of the situation to put an unreasonable burden upon the distributing company, and the mere fact that the charge is made for an interstate service does not constrain the Commission to desist from all inquiry as to its fairness. Any other rule would make possible the gravest injustice, and would tie the hands of the state authority in such fashion that it could not effectively regulate the intrastate service which unquestionably lies within its jurisdiction.

"The principles applicable in a rate investigation, where similar corporate relationship existed, were recently announced in Smith v. Illinois Bell Telephone Co., 282 U. S. 133, 152, 153, 51 S. Ct. 65, L. Ed. 255, and no purpose would be served by repetition or elaboration of what was there said." (Western Distributing Company v. Public Service Commission, 252 S. Ct. 283.)

The right of a public service commission to inquire into the cost of service rendered and gas furnished by holding or affiliated companies in determining the reasonableness of the contract is now definitely established and requires no further discussion. That is true regardless of the interstate feature of the business.

The Commission is given authority under R. S. 66-110 and R. S. 66-111 to investigate on its own motion any regu- [fol. 105] lation, classification, practice or act of a public

utility, and by R. S. 66-113 is given authority to substitute a correction therefor after such hearing and investigation, if necessary.

The Gas Service Company Contract

This is a contract between the Gas Service Company and the various distributing companies owned and controlled directly by the Gas Service Company through stock ownership. The various distributing companies own one or more, and in some instances many, operating or distributing units. The contract is made between the Gas Service Company and the distributing companies, and the latter companies are allocated a proportion of the expenses of the Gas Service Company, which purports to be the actual expenses of that company in performing the various services for the distributing companies and their operating units.

Under the contract the Gas Service Company agrees to perform certain departmental activities. For this purpose departments are maintained consisting of accounting, auditing, new business, budget, purchasing, stores, insurance, rate and valuation, legal, engineering and operating, and news functions. (Ex. 12.)

There is no dispute that services are rendered by the various departments of the Gas Service Company. All the expenses of the Gas Service Company arising from the various departments are allocated to the properties, in some instances on a customer basis in the proportion that the number of customers of each property bears the total number of customers, and in others on the basis of the relation of the revenue of each company to the aggregate revenue of all and not on the basis of services actually performed.

The Kansas City Gas Company and the Wyandotte County Gas Company do not participate in all expenses, but only in executive telephone and telegraph expenses, taxes, rent, department salaries and new business administrative expenses. The Capital Gas and Electric Company participates in all expenses except general clerical salaries, rents, welfare expenses, auditing expenses, warehouse expenses and general office supplies and expenses. The three companies above named maintain their own departments which perform the services covered by the expenses in which they do not participate.

The total expenses allocated by the Gas Service Company to all the distributing companies for the year ending June 30, 1931, amounted to $292,919.96. The Commission's ac-
[fol. 106] countants found upon examining some of the records of the Gas Service Company that there had been included in the total of $292,919.96, items aggregating $28,-972.56, which the Commission's accountants believed were not proper items of expenses to be charged against the distributing companies. The respondents thereupon prepared corrected exhibits in which the amount of expenses claimed for the year ending June 30, 1931, was reduced to $263,947.40.

These disputed items, aggregating $28,972.56, included items of legal expenses, traveling expenses, donations, memberships, subscriptions, miscellaneous expenses and incidental expenses pertaining to public relations.

The allocated expense for the year ending December 31, 1930, was submitted, and items of the same nature were questioned by the accountants for the Commission as were those submitted in the report for the year ending June 30, 1931. The controverted expenses amounted to approximately 10 per cent of the total allocated expenses.

For the purpose of eliminating any dispute and for the purpose of eliminating the necessity of a hearing upon each of the controverted items, the respondents agreed to the elimination of the expenses rejected by the accountants for the Commission.

In addition to the expenses allocated to the companies in the amounts recited above, expenses were charged directly to the distributing companies by the Gas Service Company. Such expenses charged directly to the distributing companies amounted to $101,869.78 during the twelve months ending June 30, 1931. After elimination of the disputed items the Commission does not find the amounts paid under the contract unreasonable.

The evidence discloses that under the contract the general ledger and other general books of the distributing companies are kept in Kansas City, Mo., contrary to the laws of the state of Kansas. (R. S. 17-616.) The Commission does not place any approval upon these contracts or this practice; the Commission will from time to time, as necessary, approve or disapprove any expenses which any of the distributing companies incur by reason of any services

performed by the Gas Service Company for them when credit for such expenses is claimed in rate proceedings by the distributing companies.

[fol. 107] The Henry L. Doherty and Company Contract

Henry L. Doherty and Company is Henry L. Doherty, an individual doing business as Henry L. Doherty and Company. The contract between Henry L. Doherty and Company and the various distributing companies under which Henry L. Doherty Company is paid 1¾ per cent of the distributing companies' gross revenue, an engineering fee equal to five per cent of the cost of construction, a fee for the services of the securities department, and in addition is paid the expenses, disbursements and per diem charge for Henry L. Doherty and Company's representatives while at the properties of the distributing companies, or traveling for them on special matters is as follows:

"To the Board of Directors of (the distributing company):

"GENTLEMEN: The undersigned, as fiscal agent, hereby offers to continue to place at the service of your corporation, under the same terms and conditions as have been in effect for the past several years, a complete organization which has been built up in connection with the operation and development of public utility, oil and natural gas properties, making available to you the combined experience, advice and assistance of this organization to aid you in solving such problems as may arise in connection with the conduct of your business. Among others, it is proposed to perform for your corporation, subject to the direction and control of your board of directors, the following service:

"I. Personnel. In so far as your corporation may desire, it is proposed to supply you with experienced executives and operators necessary for your business.

"II. Executive Service. Our staff of executives, financial advisers, engineers and accountants will advise and assist in franchises, rates, matters of public relations, and all matters of insurance, supervise expansion of territory and business, acquisition of additional properties, etc.

"III. General Accounting Services. Our accounting department will periodically audit the books of your corporation and generally advise in accounting problems and in

the development in accounting practices and procedure, and furnish the services of certified public accountants where special audits are required.

"IV. Statistical Services. Our statistical department will supply comparative statements of operating results of the various companies under our supervision and will also supervise or furnish statistical reports to financial institutions, government bureaus, and similar organizations.

"V. Purchasing Services. We will give you the benefit of the services of our purchasing department with regard [fol. 108] to the purchase of equipment, supplies, generally advise as to the desirable equipment, etc.

"VI. Designing and Construction Engineering. Our engineering staff will be available at all times to carry out all preliminary investigations requisite to determining the advisability of any proposed construction, will check the details of engineering design, perform engineering work where requested, and generally check the efficiency of your plant.

"VII. Financial Services. The financial department will provide plans for financing and for funds for capital requirements, including construction and additions to properties and acquisition of new properties; for the refunding of maturing obligations; will act as paying agent for coupons and dividends, and assist in the arranging of bank loans. Also, the financial department will furnish your corporation with a budget system for the advanced determination of financial requirements and operating results.

"VIII. Securities Department. The securities department will provide plans for the sale and distribution of various securities, and will formulate and carry out campaigns for sales under customer ownership plans, etc.

"IX. Valuation. The valuation department will, when required, prepare inventories and appraisals of property, and will advise as to experts who may be required to testify in valuation cases, and will generally assist in the preparation of the same.

"X. Tax Department. The tax department will prepare or supervise the preparation of federal and other tax returns and generally keep in touch with taxation problems.

"XI. New Business Department. The new business department will serve in the purchase and sale of appliances and equipment for resale, the determination of sales pol-

icies, promotion programs and sales personnel, in research and laboratory tests on domestic appliances, etc.

"XII. Technical and Research Department. The technical and research department will furnish a consulting service on all technical problems encountered by your corporation.

"Compensation. For the above services your corporation will pay as follows:

"1. A management fee equal to one and three-fourths per cent (1¾%) of its gross revenues, after deducting intercompany sales for resale.

"2. An engineering fee equal to five per cent (5%) of the cost of construction.

"3. For the services of our securities department to purchase outright blocks of securities issued by your corporation or to distribute such securities to investors, we will charge a fee to be mutually agreed upon, depending on the character of security offered and general market conditions when the offer is made.

"In addition, your corporation will pay the expenses, [fol. 109] disbursements and reasonable per diem charges for our representatives while at the properties of your corporation or traveling for it on special matters.

"The agreement will take effect as of September 1, 1929, and shall continue in effect for a period of one year thereafter and shall be automatically renewed from year to year unless terminated by either party upon written notice to the other, mailed at least ninety days prior to the end of any year.

"A resolution adopted by your board of directors, authorizing the acceptance of this offer, shall constitute acceptance thereof.

"Yours very truly, (Signed) Henry L. Doherty and Company, by Ernest H. Johnson."

In considering the reasonableness of this contract, it will be well to compare it with the contract of the Gas Service Company. A comparison discloses that the same services are contracted to be performed by both companies. The services to be performed under the Gas Service Company contract are as follows:

1. Furnish all administrative and executive service.
2. Financial aid and advice.

3. Purchasing and warehousing.
4. Engineering and operating supervision.
5. All legal services.
6. All insurance purchasing.
7. All general accounting and reports.
8. Supervision and handling of all tax matters.
9. Handling of all pay rolls.
10. Making of all audits and auditing reports.
11. Make all governmental and regulatory commission reports.
12. Supervision of all new business operations.
13. Make all vouchers and disburse funds.
14. Supervise and direct all public relations work.
15. Do all general and policy advertising.
16. Make all valuations and rates and handle all matters pertaining to rate litigation, and routine matters with regulatory bodies.
17. Make and follow up all construction and financial budgets.

If any service is performed by Henry L. Doherty and Company under the Henry L. Doherty and Company contract, it must necessarily duplicate the service to be performed under the Gas Service Company contract. This duplication of proposed service is shown, also, by a comparison of exhibit 11, which is a summary of the activities to be performed by the departments of Henry L. Doherty and Company, with exhibit 12, which is a summary of the activities to be performed by the Gas Service Company, for which services the distributing companies fully compensate the Gas Service Company.

[fol. 110] The evidence also discloses that a number of companies are operated by Henry L. Doherty and Company at 60 Wall street, which in no way, so far as the evidence shows, contribute to the defraying of the expense of the operation of Henry L. Doherty and Company.

For example: The Gas Securities Company is owned by Henry L. Doherty and Company and has its office at 60 Wall street. The company has net assets of $23,252,907. The net earnings of this company for 1929 amounted to $1,960,376. (Tr. 1650.) The witness for respondents did

not know whether any payments were made by this company to Henry L. Doherty and Company. (Tr. 1651.) No revenue is shown from this source in exhibit 16.

The Gas and Electric Securities Company is owned by Henry L. Doherty and Company and has its office at 60 Wall street. This company has net assets of $24,932,188. Its income for the year 1929 amounted to $2,086,069. (Tr. 1652.) This company is operated by Henry Doherty and Company. (Tr. 17459) Exhibit 16 shows no revenue is obtained for its operation by Henry L. Doherty and Company.

Other companies are operated by Henry L. Doherty and Company which produce no revenue for it or contribute to its expenses, including the Doherty Securities Company, the Cities Service Securities Co., which is located at 60 Wall street and has on its payroll at times between 500 and 600 employees, the Doherty Organization Investment Company, and Henry L. Doherty and Company, Inc., and so forth.

Time and space will not permit a detailed discussion of the purported activities of each department as described in Exhibit 11. Generally, the departments' activities relate principally to the purchase and sale of stock of the Cities Service Company and other companies. As an example there is a transfer department with 355 employees, which may be discussed as illustrative of some of the activities of Henry L. Doherty and Company.

The Transfer Department is composed of three sections with a personnel of 355 and the sections include:

1. Transfer Division.
2. Ledger Division.
3. Reinvestment Division.

The Transfer Division. All the Cities Service Company and subsidiaries stock, bonds and debentures are issued and transferred in this division and Henry L. Doherty [fol. 111] and Company act, not only as transfer agent for Cities Service Companies, but also for subsidiary companies such as Public Service Company of Colorado, Ohio Public Service Company, Toledo Edison Company, Arkansas Natural Gas Corporation, Indian Territory Illuminating Oil Company, and others.

In this division considerable care must be exercised in transferring securities from one owner to another. All cases involving lost and stolen securities are handled by this division and their replacement is made only after satisfactory corporate requirements are complied with.

In this division at present, approximately 120,000 certificates are transferred and issued each month.

The Transfer Division maintains a close relationship with banks and trust companies which act as cotransfer agents, registrars and trustees of many security issues of the Cities Service Company. "This division has many interesting cases presented to it in connection with stolen securities and securities obtained through fraud, as well as cases where the transfer of securities involves estates, trustees, etc."

The Ledger Division is the division in which all stockholders' ledgers are maintained and dividends distributed to stockholders. The principal stock issues maintained in this division are Cities Service Company Common, Preferred "B" and "BB" and Cities Service Power & Light Company, on which monthly dividends are paid; also other issues such as Arkansas Natural Gas Corporation, Indian Territory Illuminating Oil Company, etc.

This division also maintains stockholders' records of subsidiary companies and records carrying the names and addresses of bond and debenture holders who have registered their bonds as to principal, or principal and interest. On fully registered bonds the interest is disbursed by this division.

This division carries approximately 60,000 stock and bondholders' accounts and pays monthly dividends and interest to more than 500,000 each month. As a dividend disbursing agency, the work of this division is more complicated than the average department of this kind because monthly cash dividends are paid in addition to monthly stock dividends.

In this division the Cities Service Company common stockholders' stock dividends are sold each month in cases where an all-cash dividend is desired. "Practically the entire force of this division is engaged in working on the [fol. 112] stockholders' ledgers for the first fifteen days of each month. Then the books are closed for dividends and the balance of the month is consumed in getting out the dividends."

In the Reinvestment Division stock dividends are accumulated and cash dividends reinvested in either Cities Service Company common or preferred stock, and this division also accrues the dividends where Cities Service Company common stockholders own less than twenty shares. This reinvestment division carries approximately 370,000 accounts for stockholders for whom Henry L. Doherty and Company are either accruing dividends, reinvesting cash dividends or accumulating stock dividends.

The Cities Service Company and its subsidiaries maintain more than thirty transfer agencies and registrars throughout the United States, and the transfer department is in contact at all times with the agencies as well as with the trustees who act in connection with such bond and debenture issues.

Other activities of the transfer department relate to stockholders' lists and proxies for stockholders' meetings, rights of stockholders, conversions and exchange of debenture and bonds for stock.

Another important department is the commission department. It maintains detailed records necessary to the proper functioning of the securities department in the promotion and sale of the securities of the Cities Service Company and its subsidiaries. It has a personnel of 108 people and consists of two divisions, namely, the commission division and the reports division.

The commission division keeps records of various securities delivered against sales made through the various sales agencies of the securities department and passes on the validity of claims for commissions based on such sales and authorizes payment of commissions. It also authorizes the charge-back from time to time of such commissions as have been paid out but have not become earned.

The duties of the reports division are to make payments or to charge back commissions upon advice from the commission division and to supply itemized listings of the items on which commissions are being allowed or charged back as well as commission statements carrying the cash payments or charge-backs. It maintains accounts for the various salesmen and securities dealers to which are posted the earnings reflected by the commission's statements and the cash payments of commissions.

This division supplies the securities department, from detailed information supplied by the commission division, various statistics and reports of sell-outs, placements, etc., [fol. 113] of the various securities. The enormous activity of this department as connected with securities sales can be visualized when the statement is read, on page 22 of exhibit 11, that its duties are performed in connection with the sales activities of approximately 1,200 retail salesmen, 15,000 employees of underlying companies and 600 dealers, all engaged in the sale of Cities Service Company stock.

The office service department has a personnel of 229. It handles addressograph records of security holders for the monthly run of dividend checks and other forms in connection with stockholders ledgers. The addressograph files include approximately 700,000 plates representing security holders of the Cities Service Company, stock salesmen, employees, et cetera. About 290,000 checks and 1,000,000 statements, envelopes, and forms are turned out each month. The monthly output of graphotype machines average 40,000 names, addresses and money amount plates. Between 6,000 and 7,000 changes of addresses of security holders are required each month.

Another important department is the security holders service bureau. This bureau was created in 1923 in the interest and for the benefit of the fast-growing numbers of holders of securities of the company. (Page 65, Ex. 11.)

It has normally a staff of twenty-six, including:

Representatives who greet visiting bond and shareholders and answer their many and telegraphic inquiries.

Investigators who make careful investigation and analysis of complaints and prepare figures and facts for reply to specific questions.

Stenographers and file clerks to type and file the correspondence and records of the bureau.

The principal feature of the greeters' bureau relates to inquiries and problems of individual shareholders and bondholders of the companies' securities who visit, write or telephone to the bureau for information, advice and help, and also to afford the securities holders a channel of direct personal contact with the company and its activities.

Some idea of the vast magnitude of the operations of this department and the expense connected therewith is reflected in the statement, on page 65 of exhibit 11, that

each month since the creation of the bureau it has answered approximately 5,000 letters, and its "greeters" have greeted in its office between 1,500 and 2,500 security holders each month in addition to answering local and long distance telephone calls to the extent of many hundreds daily.

[fol. 114] The bureau cares for the correcting and changing of addresses of holders, for reregistration of securities, advice to holders of special privileges, investigates claims of nonreceipt of dividend checks, receipts, etc., cares for emergency measures to safeguard temporarily holders of lost securities until duplicate certificates may be issued, investigates complaints from shareholders and bond holders who may have given their securities to brokers or dealers who may not be responsible, and assist in means of recovery.

The bureau advises and assist in the matter of transfer of certificates in estate settlements which are apt to be complicated; secures information on outside corporations for Cities Service stockholders and furnishes security holders with literature especially prepared by the bureau for the enlightenment of the Cities Service Companies' security holders.

Other departments include foreign oil department, marine and tank car activities, oil production and pipe line department, and oil refining and marketing divisions. These departments have no relation to, nor can they be of any service to, the natural gas distributing companies.

A natural gas department and geological department may be of service and value; however, the evidence shows that Henry L. Doherty and Company is paid directly and specifically for any services of any of its employees while out engaged on work for the gas companies at a per diem rate plus expenses.

Other departments consist of an accounting department, payroll department, et cetera, whose services naturally depend upon the functions of other departments.

There is a department called "functions of finance" whose activities are related to securing capital, arranging loans and furnishing collateral when necessary. The cost of furnishing capital by the sale of securities of underlying companies is covered in the management contract as follows:

"(3) For the services of our securities department to purchase outright blocks of securities issued by your corporation or to distribute such securities to investors, we will charge a fee to be mutually agreed upon, depending on the character of security offered and general market conditions when the offer is made."

The Commission finds that the operations of Henry L. Doherty and Company are of no benefit to the distributing or pipe-line companies, except to the extent that any specific services may be rendered for which Henry L. Doherty [fol. 115] charges and collects specifically. The analysis of exhibit 11, setting out departmental activities of Henry L. Doherty and Company, shows that the contact of Henry L. Doherty and Company with the distributing companies is largely for the sole benefit of the holding company, the Cities Service Company.

An examination of the departmental activities of Henry L. Doherty and Company discloses that they are largely devoted to the purchase and sale of Cities Service Securities and details relating to the handling thereof. The Cities Service Company must pay the expense of its operation. It is not a proper charge to the expense of the subsidiary companies.

The evidence presented in this investigation as to the 1¾ per cent fee paid to the holding company by the subsidiaries discloses a modern corporate practice that should be frankly condemned. It is a scheme to take the cream from the gross earnings of the operating companies, leaving them the skimmed milk for sustenance. The money so taken for which no service is returned, may at times be the money needed to sustain the operating company—it may mean the difference between solvency and bankruptcy. This unearned money is filched from the pockets of the consumers, does not go to the stockholders, and unjustly enriches the management company. It is an immoral, if not illegal, dishonest corporate practice and will not be tolerated, much less approved by Public Service Commissions.

It further appears that any additional contact of Henry L. Doherty and Company with the distributing and pipeline companies is for the purpose of keeping Henry L. Doherty informed as to their activities and for the protection of his investment rather than for a direct benefit to the distributing and pipe-line companies. It also ap-

pears that the departments of Henry L. Doherty and Company are devoted to the extension of the investments of the Cities Service Company and Henry L. Doherty and Company, such as oil developments and others which in no way result in a benefit to the existing operating companies.

It appears that the activities of Henry L. Doherty and Company are a burden to the distributing and pipe-line companies rather than a benefit, in view of the fact that they must immediately transfer all their receipts to Henry L. Doherty and Company, leaving them dependent upon it for financial assistance for which they must pay, while Henry L. Doherty and Company has the benefit of these [fol. 116] receipts and the use of the funds of the underlying companies pending their distribution as dividends.

The relations between Henry L. Doherty and Company and the distributing and pipe-line companies places a further burden upon them due to the fact they must pay Henry L. Doherty and Company five per cent of the cost of their construction projects regardless of the benefit received or the services performed. Although this does not enter into the expense in determining a rate to be charged the consumer, it does affect the financial stability of the distributing and pipe-line companies.

The distributing and pipe-line companies, because of their relations with Henry L. Doherty and Company under this contract, have a further burden of carrying the operating expense of Henry L. Doherty and Company's securities holding companies, which were not shown to contribute to the departmental expense.

Further, because of the authority given Henry L. Doherty and Company as fiscal agent under the contract, the distributing companies are not left free to deal independently for the purchase of gas at the lowest possible price, it being the desire of Henry L. Doherty and Company to sell the pipe-line gas of its own company.

The test of the reasonableness of this contract as it relates to the 1¾ per cent payments thereunder, is to be determined by whether or not any services are actually performed for the benefit of these companies for which the companies are not billed specifically and, if so, what it costs Henry L. Doherty and Company to render this service.

There is no evidence in the record of any specific services having been performed for any of these companies by Henry L. Doherty and Company for which Henry L. Do-

herty and Company was not paid on a per diem basis and for its expenses. Practically all of the services which Henry L. Doherty and Company under its contract stands ready to perform, the evidence shows, was in fact performed by the Gas Service Company, and that the Gas Service Company was paid by the distributing companies for this service.

The evidence shows that Henry L. Doherty and Company is amply compensated for any services rendered these companies by the engineering fee, by the payment of a fee to be mutually agreed upon for services rendered by the securities department and for the direct payments for specific services performed.

From all which the Commission concludes that the fiscal [fol. 117] agency contracts between Henry L. Doherty and Company and the respondent distributing companies and the pipe-line companies are unreasonable and the amounts paid thereunder are excessive to the extent of 1¾ per cent paid on the gross receipts of these companies.

The Cities Service Gas Company Contract

This is the contract between the respondent distributing companies and the Cities Service Gas Company, under which the distributing companies purchase natural gas from the pipe-line company at the city gates. The contract is a day-to-day agreement and not in writing. In most cases the price contracted to be paid is forty cents per M. c. f. In some instances the price is lower. The average price for main line domestic gas is 39.5 cents.

The reasonableness of the contract is to be tested by what it costs the Cities Service Gas Company, the natural gas pipe-line company, to furnish gas to the affiliated distributing companies, and the rate of return earned by it on the fair value of its property used and useful in this service. This will involve a consideration of the following factors:

1. The fair value of the pipe-line system used and useful in service, exclusive of gas leases.
2. The present fair value of the gas leases, used and and useful.
3. A proper allowance for annual depreciation and depletion.

4. The net earnings of the company available for annual return.

5. The fair rate of return.

These factors will be considered in the order set out above.

The Fair Value of the Pipe-line System Used and Useful in Service

In arriving at the value of the pipe-line system used and useful in service, the Commission has the valuation submitted by Mr. Hamilton, engineer for the respondents, the testimony of Mr. Eastman in support of Mr. Hamilton's exhibit, and the valuation submitted by Mr. Black, the engineer for the Commission.

Both Mr. Black and Mr. Hamilton have followed the same classification of accounts, but it is possible that some property classified by Mr. Black under Account 1314, Production field-line equipment, may have been classified by Mr. Hamilton under Account 1333, Transmission-line equipment, or vice versa. Mr. Black classifies certain rights of way under Account 1307, Production rights of way, whereas Mr. Hamilton shows nothing in this account. Both engi- [fol. 118] neers worked with approximately the same inventory of property items, and it is apparent all property has been included by both, in some classification.

The classification of accounts, by account number and description, is shown by the following tabulation.

Acct. No.	Description.
1301.....	Organization.
1307.....	Production—rights of way.
1310.....	Production—field measuring station structures.
1311.....	Production—other structures.
1312.....	Production—gas-well construction.
1313.....	Production—gas-well equipment.
1314.....	Production—field-line equipment.
1315.....	Production—field measuring-station equipment.
1316.....	Production—drilling and cleaning equipment.
1317.....	Production—other equipment.
1325.....	Transmission—land.
1327.....	Transmission—rights of way.
1328.....	Transmission—compressing station structures.
1329.....	Transmission—measuring station structures.
1330.....	Transmission—other structures.
1331.....	Transmission—compressing station equipment.
1332.....	Transmission—measuring station equipment.
1333.....	Transmission—line equipment.
1334.....	Transmission—other equipment.

Acct. No.	Description.
1376	General—other land.
1379	General—other structures.
1380	General—office equipment.
1381	General—store equipment.
1382	General—shop equipment.
1383	General—stable equipment.
1384	General—garage equipment.
1385	General—laboratory equipment.
1386	General—telephone and telegraph system.
1387	General—tools and implements.
1388	General—other equipment.
1390	Engineering and superintendence.
1391	Law expenditures during construction.
1993	Taxes during construction.
1394	Interest during construction.
1395	Miscellaneous construction expenditures.
	Cost of financing.
	Working capital.
	Material and supplies.
	Going concern value.

The valuation of nine of these accounts is not disputed by the engineers, and the Commission, therefore, adopts their value as follows:

Acct. No.		Repro. cost, new.	Repro. cost, new, less dep'n.
1316	Production—drilling and cleaning equipment	$32,833	$27,908
1376	General—other land	3,655	3,655
1380	General—office equipment	117,817	106,035
1381	General—store equipment	2,123	1,805
1382	General—shop equipment	26,991	23,084
1383	General—stable equipment	640	568
1385	General—laboratory equipment	8,369	8,202
1387	General—tools and implements	51,358	44,979
1388	General—other equipment	23,877	21,832

[fol. 119] The remainder of these accounts will be discussed under the order in which they appear in the classification, with the exception of Account 1301, which will be discussed under the heading Intangible Items which follows the discussion of Tangible Items.

Account No. 1307

Production—Rights of Way

This account includes rights of way on production field lines, as distinguished from transmission lines, valued by Mr. Black at $33,990. This right of way is valued at $0.85 per rod.

Mr. Hamilton does not show any rights of way under this classification, but he may have included this under Account

No. 1327, Transmission—rights of way. A comparison of exhibits 41A, B and C, and exhibits 17A and B, shows that Mr. Black has allowed a total of 1,212,251 rods for rights of way in Accounts 1307 and 1327, as compared to Mr. Hamilton's allowance of 1,180,102 rods in Account 1327. In other words, Mr. Black has allowed an excess over Mr. Hamilton of 32,149 rods of rights of way.

It is our opinion that an allowance under this account is proper. We find that the fair average value per rod of pipe-line right of way in this system is $1.40, which applied to the 39,987 rods of right of way allocated by Mr. Black to this account, gives $55,982 as the fair value of this account. The development of this average unit price of $1.40 per rod for production rights of way is discussed under Account 1327, Transmission—rights of way.

Account No. 1310

Production—Field-Measuring Station Structures

This account includes the buildings and appurtenant constructions housing meters, regulators, and other field measuring equipment, as distinguished from similar structures housing equipment measuring gas delivered by transmission system lines to city gates or other users. These structures are valued by Mr. Black at $40,517, cost of reproduction new, and $35,909 depreciated. Generally the structures covered by this account are sheet metal on wood frames with no foundations and dirt floor. They range from 3 x 5 x 3 feet to 10 x 12 x 8 feet in size, the average size approximating 6 x 8 x 7 feet. Mr. Black's valuation lists 597 of these structures, 43 of which are carried as one item. The average cost per structure is $68 new, and $60 depreciated. Mr. Black testified (Tr. 1777) that in pricing these structures [fol. 120] they were separated into classes by size and type of construction, detailed estimate of materials and costs were worked out for each class, and then the cost applied on a cubic-foot basis.

These structures are valued by Mr. Hamilton at $42,244 new, and $37,194 depreciated. Mr. Hamilton furnished no detail of value of individual structures.

The company introduced exhibit 54 (Tr. 2045), showing in part alleged omissions from Mr. Black's valuation, of twelve meter settings and housings which should properly

be classified under Accounts 1310 and 1315. No separation was made as between these accounts, and the amounts claimed by the company are added in Account 1315.

In pricing these structures, Mr. Black separated them into classes, by size and type of construction, and worked out a detailed estimate of materials and costs for each class in arriving at his cubic-foot basis, and he sets up individual structures in this account on approximately 120 pages of exhibits 41-A, B and C. Mr. Hamilton sets out the value of this account in a lump sum without any detail and without even setting out the number of structures and valuation. He claims to have arrived at his cubic-foot basis upon the experience of many years, but does not give the Commission any data which may have been accumulated by reason of this experience.

Mr. Black and Mr. Hamilton arrived at approximately the same per cent condition for the items in this account. Mr. Black found the cost new, less depreciation, to be $35,909. Mr. Hamilton found the cost new, less depreciation, to be $37,194, or a difference of $1,285.

Mr. Black and Mr. Hamilton, in arriving at the present value of this account, have done so by inspection of the property.

Counsel for the Commission suggest that—

"Inasmuch as this property is dependent upon the life of the gas fields in which it is used, the per cent condition of this account should be based upon the proportion which the recoverable gas in the fields bears to the total of the reserves estimated originally in these fields."

Their basis of arriving at the depreciated value by the depletion method is set out for the purpose of discussion as follows:

"After eliminating storage fields, and making allowance for salvage, we have made a calculation of the present fair value of the property in this account on this basis, excepting in the state of Texas, where it appears from the evidence that the life of the field will equal or exceed that of the property in this account.

[fol. 121] "The development of the present fair value of Account 1310 by depreciating in ratio with depletion of gas fields in Kansas (exclusive of Augusta and Craig fields), Missouri and Oklahoma, and by inspection methods

in Texas, and Augusta and Craig fields in Kansas, is computed as follows:

"Mr. Eastman's exhibit 39 sets out the estimated salvage for Accounts 1310 and 1315 combined, which includes both structures and equipment. In Kansas the estimated salvage of these two accounts (exclusive of Augusta and Craig fields) is $18,275, and the reproduction cost new is $234,303. The estimated salvage is computed as 7.8 per cent of the reproduction cost new. In Missouri the reproduction cost new is $3,997, and the estimated salvage is $500, being 12.5 per cent of the reproduction cost new. In Oklahoma the reproduction cost new is $128,433 and the estimated salvage is $10,415, which is 8.11 per cent of the reproduction cost new.

"Mr. Davis' exhibit 3, pages 60 and 61, sets out the ultimate gas reserves and the reserves as of July 1, 1931, in M cubic feet. In Kansas (exclusive of Augusta and Craig fields) the ultimate reserves are 39,207,458 M cubic feet, and the reserves as of July 1, 1931, are 8,222,000 M cubic feet, which is 20.97 per cent of the ultimate reserves, or a weighted average per cent condition of the fields in Kansas (exclusive of Augusta and Craig fields).

"In Missouri the ultimate reserves are given as 46,648 M cubic feet, and the reserves as of July 1, 1931, as 25,000 M cubic feet. Dividing 25,000 by 46,648, the weighed average per cent condition of the Missouri fields is found to be 53.59. In Oklahoma the ultimate reserves are given as 65,001,665 M cubic feet, and the reserves as of July 1, 1931, as 14,633,000 M cubic feet. Dividing 14,633,000 by 65,001,665 the weighted average per cent condition of the Oklahoma fields is found to be 22.51.

"Taking the adopted reproduction cost new on Kansas (exclusive of Augusta and Craig fields) of $18,839, and deducting 7.8 per cent as computed from Eastman's exhibit 39, as salvage, we find the reproduction cost new, less estimated salvage, to be $17,370. To this figure of $17,370, we apply the per cent condition of 20.97, as developed from Davis' exhibit 3, and arrive at a depreciated value, less salvage of $3,642, to which the estimated salvage of $1,469 is added, giving a present fair value for Kansas (exclusive of Augusta and Craig fields) of $5,111. In the Augusta and Craig fields we have used Black's depreciated value of $4,598 arrived at by inspection. In Missouri we have taken

the adopted reproduction cost new of $280 and deducted 12.5 per cent salvage, computed from Eastman's exhibit 39, and find that the reproduction cost new, less salvage, is $245. To this figure of $245, we apply the per cent condition of 53,59, as developed from Davis' exhibit 3, and arrive at a depreciated value, less salvage, of $131, to which the estimated salvage of $35 is added, giving a present fair value for Missouri of $166.

"In Oklahoma we have taken the adopted reproduction cost new of $10,332 and deducted 8.11 per cent salvage, computed from Eastman's exhibit 39, and find that the [fol. 122] reproduction cost new, less salvage, is $9,494. To this figure of $9,494 we apply the per cent condition of 22.51, as developed from Davis' exhibit 3, and arrive at a depreciated value, less salvage, of $2,137, to which the estimated salvage of $838 is added, giving a present fair value for Oklahoma of $2,975.

"In Texas we have adopted Black's depreciated value of $5,721, arrived at by inspection.

"Adding together the present fair values found for each of the several states, the present fair value for Account 1310 is $18,571 if the present fair value is computed by this method."

This theory does appear to us to be a fair and reasonable basis for determining the present fair value of the property, inasmuch as the property is dependent upon the life of the gas fields in which it is used, and the value of the equipment is returned to the company by amortization and depletion allowance upon such basis. We do not believe, however, that the proper result can be reached by taking the property of the company in the states as a whole and using only the reserves which the company owns for the purpose of this calculation. We are unable to find in the record sufficient evidence upon which to allocate the property to each particular gas reserve, and, therefore, decline to apply this theory of depreciation to the pipe-line property. We might add in passing that if it were possible from the evidence to use this method of depreciation that it would also apply to Accounts 1311, 1312, 1313, 1314, 1315 and 1317, decreasing the present value of the property approximately two million dollars.

We find the cost of reproduction new to be $40,517 and the value of Account 1310 to be $35,909.

Account No. 1311

Production—Other Structures

This account is valued by Mr. Black at $59,087 new and $47,876 depreciated. The account covers sixty-six warehouses, dwellings and miscellaneous structures and includes fences, sidewalks and other improvements.

In Hamilton's appraisal this account is valued at $60,832 new, and $50,162 depreciated, and covers the same number of structures as shown by Black. Mr. Eastman testified with respect to this account (Tr. 1108, 1114-1122) that he arrived at a 16c per cubic foot value for the structures based on his general experience. We find the present cost of reproduction new to be $59,087 and the present fair value of this account to be $47,876.

[fol. 123] Account No. 1312

Production—Gas-well Construction

This account is valued by Mr. Black at $1,718,813 new, and $1,210,392 depreciated. This account covers all costs of drilling gas wells, and the placing in the wells of all casing, tubing and equipment furnished by the owner. The number of wells, location, and the items entering into their construction was taken by Black from an inventory furnished by the company.

Mr. Black's development of unit cost is illustrated by his testimony with respect to Fuqua Well No. 2. He testified that the allowance for items in this account was broken down into a unit price per foot for the contract drilling on gas wells; and that in addition allowances had been made for day work, for fuel, for water, for depreciation of casing withdrawn and used, for transportation of casing and tubing and for superintendence during the drilling period. A. S. Ritchie also testified with respect to drilling costs estimated by him on Fuqua No. 2 and Burnett No. 14.

A comparison of Mr. Black's, Mr. Hamilton's and Mr. Ritchie's valuations of certain wells, completely equipped is found on transcript page 2891, and follows herewith:

			Ritchie	
Well	Black	Hamilton	Standard rig	Rotary
Fuqua No. 2	$19,843	$24,991	$22,303	$22,101
Burnett No. 14	30,024	32,847	27,301	23,779

The property in this account is valued by Mr. Hamilton at $2,022,296 new, and $1,300,025 depreciated.

In support of the cost of reproduction new used in Hamilton's appraisal, the gas company introduced, as exhibits 65 to 70, inclusive, photographs of job orders and vouchers covering Fish No. 2, Charty No. 2, Freyler No. 1 and No. 2, and Fuqua No. 2. Mr. Eastman's development of unit costs per foot of drilling was developed from the company's experience in drilling in these various fields, and no testimony covering the details of the development other than the actual cost to the company for the drilling of these wells originally was ever introduced by Mr. Eastman or Mr. Hamilton. Original costs were introduced, letters from other gas companies covering cost of wells drilled in approximately the same territory were introduced, but at no time was any breakdown of the figures used by Mr. Hamilton in his exhibit 41A ever given in response to examination of the company's witnesses.

In addition to the matters above mentioned reflecting on [fol. 124] the value to be allowed for this account, our judgment is influenced by another consideration. Mr. Ritchie, production manager for the Derby Oil Company and theretofore production and pipe-line superintendent of the Marland Oil Company, having had fourteen years experience in drilling and contracting wells in Kansas, Oklahoma, Texas, New Mexico and California, testified that he was familiar with costs of drilling wells in the Amarillo Proven Sweet Gas Fields in September, 1931; that by use of rotary tools, wells could be drilled in this field at this time at a less cost than if standard tools were used, and that the Fuqua well No. 2 and the Burnett well No. 14, concerning which respondents introduced testimony as to their actual cost, could be completed at what is known as turnkey job prices as follows: The Fuqua well No. 2 at $22,303 with standard and $22,101 with rotary tools; and that the Burnett well No. 14 could be completed for $27,301 with standard and $23,770 with rotary tools. Mr. Black's complete costs on these two wells are as follows: Fuqua well, $19,843 and Burnet well No. 14, $30,024, and total considerably more than it would actually cost to complete these wells, as testified to by Mr. Ritchie. We are of the opinion that Mr.

Ritchie is a man of wide experience in this kind of work. He testified that the estimate of cost of these wells as given by him were estimates on which he would be willing to contract to complete the wells and we believe they are accurate. In addition he stated that if he had twenty wells to drill his cost would be reduced five per cent. The evidence here shows that in the Amarillo field respondents have sixty wells and it is fair to presume that in the case of a contractor taking a contract to drill sixty wells, a deduction of more than five per cent might be made. We think it is fair to use the figures given by Mr. Black as the reproduction value of these wells, inasmuch as they are higher than those given by Mr. Ritchie, and this applies to the total valuation as found by Mr. Black. Mr. Black found a cost of reproduction new for this account in the amount of $1,718,813. This account includes storage wells in the Craig and Augusta fields. The reproduction cost new given these storage wells by Mr. Black, totaled $130,363. It is our opinion that the value given these wells should be deducted from this account. A storage well is one which was formerly drilled for gas and has been abandoned for that purpose after the gas is depleted. The record shows that the respondents have two fields which they use for storage, one known as the Craig field and the other as the Augusta field. These fields are used as a reservoir into which gas is placed [fol. 125] during the summer months when the demand for gas is low, as a reserve to be used when the demand is greater. The record shows that the company, after the gas in those particular fields was exhausted, entered into contracts with the land owners whereby they leased these lands and these abandoned wells for storage purposes. We believe that these abandoned wells (referring only to the hole) belong to the landowners and not to the company and that they are simply leased to the company for the purposes mentioned in the storage contract, and that the company has no title to them and they should not be included in the valuation of respondents' property. We have, therefore, decreased Mr. Black's reproduction new value for this account of $1,718,813 by $130,363, or to $1,588,450. We find the present fair value of this account to be $1,153,157.

Account No. 1313

Production—Gas-well Equipment

This account covers all casing, tubing and fittings in the wells. The account is valued by Mr. Black at $658,245 new and $484,514 depreciated. The inventory of these items was furnished by the company and unit prices were applied developed by Black.

Mr. Hamilton values this account at $917,777 cost of reproduction new, and $573,124 cost of reproduction depreciated.

The testimony with respect to the allowances for casing and tubing included in this account is apparently conclusive with respect to the prices fixed by Black being insufficient, while the testimony is not conclusive that the prices used by Mr. Hamilton were representative prices as of the date of his valuation. However, we have accepted his total of $653,309 for casing and tubing in this account, corrected for overheads which we believe to be excessive, and have applied instead the overheads used by Mr. Black. The net difference in the allowance for casing and tubing at the site of the wells between Mr. Hamilton's and Mr. Black's valuations is $288,617, including overhead.

The testimony with respect to allowances for casing and tubing included in this account was emphatic with respect to the purchase of such materials from local supply houses because of the necessity of immediate delivery when the need for such supplies developed. However, the overhead allowances included by Mr. Hamilton were made up of two items, 5 per cent for warehousing and an additional 5 per cent calculated on the price of casing and tubing plus ware- [fol. 126] housing, for omissions and contingencies, or a total of 10.25 per cent on the price of these materials. Mr. Black allowed in his exhibit 42, "Unit Cost Analysis," a total of 3½ per cent structural overheads on pipe and casing made up by an allowance for omissions and contingencies of ½ per cent, 1 per cent for purchasing, ½ per cent for supervision and inspection. These allowances we find to be proper and ample. We have, therefore, corrected this account by using Mr. Hamilton's prices for casing and tubing to which we have applied Mr. Black's overhead percentages, giving a cost of reproduction new of $894,618 for this

account. Applying the per cent condition used by Mr. Black of 73.6 per cent, we find a cost new, less depreciation, of $658,439.

Account No. 1314

Production—Field-line Equipment

This account covers the labor and materials necessary to construct and test pipe lines between the wells and the transmission system. The account is valued by Mr. Black at $3,548,102 new, and $3,126,159 depreciated. Items in this inventory were taken from the pipe-line maps of the company. Prices of pipe, materials and labor developed by Mr. Black have been used in arriving at the total of this account. In Texas, gathering lines up to and including four-inch were priced on the basis of being buried at half the depth of main line. In other states gathering lines up to and including 12¾-inch were considered as being placed in trenches half the depth of main line of the same size. Mr. Black testified that this assumption was fair and that throughout the system there were 747,000 feet of gathering lines and 230,000 feet of transmission system mains above ground, but that the lack of time had prevented the accurate location of such lines, and they were all considered as being in trench and were so priced.

Mr. Hamilton values this account at $4,447,806 reproduction cost new and $4,169,763 depreciated. From an examination of Mr. Hamilton's exhibit it appears that there is a difference of opinion concerning lines falling in Account 1314, Producton—Field Line Equipment, and Account 1333, Transmission Line Equipment. Mr. Black may have included in one account what Mr. Hamilton may have included in another, but the lines allocated to both accounts comprise the entire system of field and transmission lines.

Consideration of this Account 1314 involves an analysis of cost of pipe, excavating and back-filling, pipe laying and [fol. 127] all other elements of cost appearing in Account 1333. Each of the items involved covers considerable space in the record, and the situation is simplified by considering the items common to both accounts and making such modifications as appear proper at one time, and these matters will be discussed later. We choose to follow counsel's suggestion and to consider any adjustment in pipe prices under

Account 1333. Respondents question counsel's attempted corrections of pipe prices in this account of page 28 of their reply brief, stating that they will discuss the matter when they reach Account 1333. We are, however, unable to find any assistance in adjusting pipe prices from further discussion in respondent's reply brief. We find the reasonable value of this account to be $3,548,102 new, and the present value of this account to be $3,126,159.

Account No. 1315

Production—Field Measuring-station Equipment

This account is valued by Mr. Black at $298,526 new and $261,887 depreciated. This account covers all measuring equipment, valves, pipes and fittings, not a part of production field line equipment, for measuring of gas in the field.

Mr. Hamilton values this account at $402,535 new, and $385,746 depreciated. There is no detail of this account in Mr. Hamilton's exhibits other than total costs of reproduction by fields, excepting where the number and unit prices of meters are indicated; there is, therefore, no way to check the number of installations covered by Mr. Hamilton's exhibit. The company introduced exhibit 54 (Tr. 2045) and called Mr. Black's attention to the alleged omission of fifty-one stations from Mr. Black's inventory, which was detailed so individual stations could be checked against it. These stations were never identified by Mr. Black and there is no testimony showing that they were included or excluded in this account, or that they were in fact in existence at the time of his inspection. The gas company's inventory, as stated before, shows no detail with respect to these stations, so exhibit 54 cannot be checked against Mr. Hamilton's exhibit.

The company claimed that these fifty-one stations total $27,865 new, and in order to eliminate any argument concerning whether they have or have not been included in Mr. Black's valuation, we are adding $27,865 to his reproduction cost new in Accounts 1315 and 1332. Exhibit 54 does not separate these stations between Accounts 1310 and 1315, 1329 and 1332.

[fol. 128] We have added to Mr. Black's reproduction new, of $298,526 for this account, $4,085.00 claimed by the company for the twelve stations omitted from Accounts

1310 and 1315, and find a cost of reproduction new for this Account 1315, of $302,611. We have added to Mr. Black's present fair value of this account of $261,887, the company's depreciated value for these stations of $3,859, making a total of $265,746, which we find to be the present fair value of this account.

Account No. 1317

Production—Other Equipment

This account consists of water tanks, water wells and one windmill used in connection with the company's production operations. It is valued by Mr. Black at $1,501 new, and $1,206 depreciated.

Mr. Hamilton valued this account at $1,774 new, and $1,461 depreciated.

On consideration of this account and the fact that there is little difference between the valuations of Mr. Hamilton and Mr. Black and the evidence on the valuation, which is not detailed and no unit values given, we find that the fair value of this property is $1,637 new, and $1,333 depreciated.

Account No. 1325

Transmission—Land

This account is valued by Mr. Black at $149,202, and is undepreciated. The company appraised all real estate for the purpose of this valuation and furnished the above total to Mr. Black, and it was adopted by him without check. This land in general is occupied by compressing stations, meter stations and other miscellaneous structures required in the operation of the transmission system. It comprises all land owned in fee by the company with the exception of Account 1376, General—Other Lands, which includes a telephone office site at Douglass, Kan., warehouse sites at Caney, El Dorado, Emporia, Petrolia and Tyro, Kan., and a meter shop location at Bartlesville, Okla.

The testimony in this case is conclusive to the effect that the Hominy, Owasso and Hogshooter compressing stations have not been used for several years and are not now used or useful in the operation of this system. We have there-

fore deducted $4,000 for compressing station sites at Owasso and Hogshooter, and find the present fair value for this account of $145,202.

[fol. 129] Account No. 1327

Transmission—Rights of Way

This account covers both pipe-line and telephone-line rights of way. It is valued at $1,174,574, and is not depreciated.

Mr. Black allowed in Accounts 1307 and 1327 for 1,212,251 rods over Mr. Hamilton's allowance of 1,180,102 rods. Mr. Black also allowed in Account 1327 for 65,440 rods of telephone-line rights of way, an excess of 50 rods over Mr. Hamilton's allowance of 65,390. Mr. Black allowed 85 cents per rod for pipe-line rights of way on pipe lines under 16-inch, and $1.20 per rod for pipe-line rights of way for lines over 16-inch, and 25 cents per rod for telephone-line rights of way. His prices were predicated (Tr. 2164) on studies of right of way cost data in Texas, Oklahoma, Kansas and Missouri, and were based both on cost of rights of way (Tr. 2164) in Oklahoma and Kansas, and on valuation costs of the Lone Star Gas Company in Texas and Oklahoma; the Oklahoma Natural Gas Company in Oklahoma; the Oklahoma Power and Water Company valuation in Oklahoma; the Panhandle Eastern and the Panhandle Illinois Pipe-Line Company in Kansas and Missouri. Mr. Black's breakdown of unit cost allowance for rights of way (Tr. 2167) allowed the following items and amounts:

Cost of right of way, 50 cents per rod.

Damages and fencing for lines under 16-inch, 20 cents.

Damages and fencing for lines 16-inch and over, 45 cents.

Cost of securing right of way for lines under 16-inch, 15 cents.

Cost of securing right of way for 16-inch and over, 24 cents.

Mr. Black's allowances also included all items of expense involved in the securing and recording of deeds and making the necessary transactions. It also included abstracting and notary's fees. These figures are developed (Tr. 2168) as follows:

Cost of securing right of way, 88 men working over a four-month period at $500 per month	$176,000
Allowance for transportation	4,000
Legal expenses	12,000
Miscellaneous expenses	10,000
Total	$202,000

Mr. Black considered that there would be in round numbers 3,000 miles of right of way, which divided into $202,000 gives a figure of 21 cents per rod for cost of securing rights of way. He allowed a cost, therefore of 15 cents per rod for securing rights of way on the smaller lines and 25 cents on the larger lines. Mr. Black's average allowance [fol. 130] per rod for pipe-line rights of way in Accounts 1307 and 1327 is $1,208,564 divided by 1,212,251 rods, $0.997 per rod.

Mr. Montgomery (Tr. 2768) introduced exhibit 87 showing the cost to the company of rights of way acquired on some twenty pipe lines. This exhibit covers a total of 6,215,512 feet of line; the right of way and damage costs totaled $407,179.82, or an average cost of $1.08 per rod. The rods of right of way covered in Montgomery's exhibit total 376,698, or 31 per cent of the total of 1,212,251 rods of right of way in Accounts 1307 and 1327. Of the total rods of right of way covered by Mr. Montgomery's exhibit 87, 171,638 rods are for lines under 16-inch and 205,060 rods for lines 16-inch and over. Applying Mr. Black's allowances of 85 cents per rod and $1.20 per rod, his allowance for the right of way in this exhibit is $391,964, or $15,216 less than cost of right of way and damages of $407,179.82, shown by Mr. Montgomery's exhibit 87. The right of way secured for the lines covered by this exhibit 87 covered the period from April, 1928, to October, 1931, and costs thereof were probably in excess of those obtaining at the time of this inquiry, due to decreased values.

Respondents contend that Mr. Montgomery's figures were obtained from analysis of job orders which do not contain all of the items of cost such as legal work in connection with securing rights of way, notary fees, et cetera.

An allocation of all the expense of the pipe-line company entering into these accounts indicates that the addition, because of these items, would add very little to the rights of way cost.

Mr. Hamilton's value on this account is $3,696,804. Mr. Hamilton's value per rod for pipe-line right of way averaged $3.25 per rod in Kansas, $3.27 per rod in Missouri, $3.27 per rod in Nebraska, $3.12 per rod in Oklahoma and $2.11 per rod in Texas. Transmission rights of way on the lines of the Cities Service Gas Pipe Line Company in Kansas averaged $2.43 per rod, and in Oklahoma and Texas $2.11 per rod. Mr. Hamilton's exhibit includes pipe-line rights of way of the American Pipe Line Company in Kansas and Missouri, $3.45 per rod. Mr. Eastman testified that in the figures quoted above, all costs incident to obtaining the right of way and in preparing it up to the point when the pipe line is laid, together with all settlement for damage claims arising from the laying of the lines, were included, and on transcript page 1286 he named the following items: Aerial surveys, 10 cents per rod; field survey in staking the route of a line, 19 cents per rod; right of way payments for purchase or easements from landowners, [fol. 131] $1.25 per rod; crop damages, damages to fences and trees, 70 cents per rod; expense of obtaining right-of-way agreements; 30 cents per rod; abstracting and recording of rights-of-way agreements, 10 cents per rod; miscellaneous expense, 10 cents per rod; clearing, grading and fences, 80 cents per rod, making a total of $3.54 per rod.

Lower costs were testified to by Mr. Eastman in Cowley county, Kansas, where a cost of $2.86 was used; Mr. Eastman testified that these costs were predicated on actual experience of the Cities Service Gas Company and other pipe-line companies of which he has knowledge, including the Continental Construction Company pipe line from the Texas fields to Joliet, Ill., and on transcript, page 1290 he testified that his costs were based primarily on the experience of the Continental Construction Company and on the experience of the Cities Service Gas Company on certain lines that have been recently laid, but he furnished no data as to the experience of any of these companies.

The company introduced two other witnesses who testified on the cost of right of way. J. S. Gibson, right-of-way agent for the Prairie Pipe Line Company, testified to nothing specific excepting that he considered the allowance by Mr. Black to be too low.

We do not believe that the allowance made by Mr. Hamilton for aerial survey is proper. The line was constructed

with the advantage of an aerial survey. As this line has been constructed without an aerial survey it would be improper to allow the cost of an aerial survey and in addition the increased costs in the valuation due to the fact that an aerial survey has not been made, and would not be used in reproducing the company's pipe line along a route already determined.

If the present cost of reproducing the pipe line is greater because in laying it over it did not have the advantage of an aerial survey it would certainly be improper to allow the additional cost of an aerial survey.

Mr. Hamilton also makes an allowance for grading and fencing. Mr. Black has made this allowance under his construction cost. From the testimony of the witnesses we believe this to be the proper place to handle this item.

Mr. Hamilton makes an allowance for legal expense under legal expense during construction. He testified that, "That would include all of the legal expenditures for the incorporation, and for the drawing of contracts, for all of the type of work that must be done prior and during the con- [fol. 132] struction of the property." (Tr. 1541.) It would therefore be improper to include legal expense in the cost of obtaining rights of way. Mr. Montgomery submitted exhibit 87, showing the actual cost of acquiring rights of way, to the company, on over 31 per cent of the line in controversy, to be $1.08. The company's contention is that the exhibit prepared by Mr. Montgomery from the company's job orders does not include all the costs of acquisition of the rights of way, such as going out and securing right of way, securing abstracts and recording them, including the expense of the men in the field, the automobile expense, telephone calls, legal expense and locating rights of way.

Mr. Black's average cost per rod of the whole system is 99 cents. This figure is 9 cents below the actual cost to the company, as reflected by the job orders. This cost of $1.08 occurred during the years 1928, 1929, 1930 and 1931. This must be recognized as a period of high prices and expensive pipe-line construction, and it is reasonable to assume that the prices at that time were influenced upward by those existing conditions.

Mr. Black has included engineering and staking out under the engineering account, No. 1390. The cost of clearing,

grading and construction damages have been included under construction cost. These items appear to be properly included in these accounts under the practice of the company. Exhibit 38 consists of one of the construction contracts under which the contractor agrees to perform the following services: Clearing the right of way before construction and cleaning up right of way after the completion of the work, to make all repairs to fences, and all cost of other improvement damages.

"Such damages for which the contractor is responsible includes repairs to fences, hedges and roads, and damage done to or by stock escaping through fences or gates left open or insecurely closed, as well as any and all damages to stock on account of being frightened, damage due to cutting hedges, damages to travelers in horse-drawn or automotive equipment, or stock, caused by open ditches, and in general any damages that might have been avoided by care on the part of the contractor. All such claims for damages for which the contractor is liable shall be settled by the contractor." (Ex. 38.)

This contract also provides that the contractor is to receive construction material furnished by the company at rail points closest the work and to transport such material used in excavation and construction of the pipe line and back fill for certain stipulated prices. Grading of the rights of way, which is a construction cost, is not mentioned in the [fol. 133] items which the company is to furnish or perform for the contractor, and is included as an item incidental to excavation.

In view of Mr. Montgomery's analysis of rights-of-way costs, we are of the opinion that Mr. Black's allowances should be increased to an average over the entire system of $1.40 per rod to cover all costs of acquisition, damages and other incidental costs chargeable directly to right-of-way cost. We have, therefore, allowed for Account 1307, Production—Right of way, 39,987 rods at this average price of $1.40 and have carried this total for Account 1307 as $55,982. We believe the total fair value for pipe-line right of way in Account 1327 to be $1,641,170, and for telephone rights of way to be $16,360, or a total for Account 1327 of $1,657,530. In arriving at this figure we have applied an average price of $1.40 per rod to 1,172,264 rods of pipe-line

right of way and a price of 25 cents per rod to 65,440 rods of telephone line.

We have arrived at the figure of $1.40 per rod by taking the actual average cost of right of way and damages of $1.08, as shown by the books of the company, and have added thereto 22 cents per rod for expense of acquisition and 10 cents per rod for the expense of abstracting and recording, which is the average cost of these items as testified to by Mr. Hicks, the right-of-way agent for the company.

We find the present fair value of Account 1327 to be $1,657,530.

Account No. 1328

Transmission—Compressor-station Structures

This account includes all structures and appurtenant construction for compressing station operation, including dwellings, garages, machine shops, dams and buildings housing compressors.

The account is valued by Mr. Black at $1,806,823 new and $1,567,605 depreciated. In pricing these structures Mr. Black had available detailed drawings on important structures, and also such information as was contained in the company's exhibit 17. Inspection was made in the fields of all structures in this account, sizes were checked, bills of material were prepared, and the prices applied were carefully developed for all structures of a given type; on patented buildings, much of the data with respect to cost were developed directly from the manufacturer.

This account is valued by Mr. Hamilton at $2,482,629 new and $2,267,443 depreciated.

There is no detail in Mr. Hamilton's valuation of the cost [fol. 134] of major items such as buildings, the unit cost appearing in each case being a total for a building. For example, on page 116 of his exhibit 17B, the first item at the top of the page is the main compressor building at the Wichita station. The building is described as being 69′ 6″ x 229′ 3″ x 35′ 0″; foundation, concrete and bricks; walls and roofs, corrugated steel; floors, concrete; unit cost, $72,494.63.

The testimony of Mr. Eastman in support of these lump-sum costs was that they had been arrived at by applying a

cubic-foot unit price to the volume of the building and that such unit costs had been developed through the company's experience in construction, and that no further breakdown was possible excepting to separate superstructures and foundations. Contrasted with such testimony, Mr. Black testified in minute detail concerning his development of labor, materials, and overhead costs and his method of applying them to items of material entering into the construction of such structures.

W. D. Truman, construction engineer for the Kansas City Structural Steel Company, and George P. Reintjes, a contractor of Kansas City, testified on behalf of the company. Mr. Truman made estimates of cost of the main structures at five compressing stations, by using estimates prepared by Mr. Reintjes on the foundations of these structures, and adding superstructure costs developed by himself. His estimates covered roughly 32 per cent of the total cost of these structures as estimated, and Mr. Reintjes estimated approximately 68 per cent of the total. Mr. Truman testified (Tr. 2336-2341) that he estimated the cost of the main compressing station buildings of the company at Higgins, Tallant, Drumright, Ottawa and Grabham. That he estimated superstructures only, and that all excavation and concrete foundations, electric lighting and other construction was estimated by George P. Reintjes, of Kansas City, and the figures furnished him were added to his estimates of superstructures in order to get the total for each structure. Mr. Truman compared these estimates with the values found for the same structures by Mr. Black. That comparison follows

Station.	Black's valuation.	Truman's valuation.
Higgins	$38,010.00	$64,115.00
Tallant	26,953.00	43,885.56
Drumright	23,610.00	46,679.98
Ottawa	40,232.00	52,677.49
Grabham	51,601.00	77,197.00

[fol. 135] Mr. Reintjes testified (Tr. 2350) that he estimated the foundations, gave his figures to Mr. Truman, and that by subtracting his figures Mr. Truman's superstructures allowances could be determined. This operation is shown by the following table:

Station	Truman's valuation, including Reintjes' estimates	Reintjes' estimate of foundations, etc.	Truman's valuation of superstructures
Higgins	$64,115.00	$45,400.00	$18,715.00
Tallant	43,885.56	29,403.56	14,482.00
Drumright	46,679.98	36,313.58	10,366.40
Ottawa	52,677.40	34,924.00	17,753.40
Grabham	77,197.00	49,410.36	27,786.64

Mr. Black (Tr. 2473, 2474) compared his valuation of the superstructures with the valuation by Mr. Truman as follows:

Station	Truman's valuation of superstructure	Black's valuation of superstructure
Higgins	$18,715.00	$18,530.11
Tallant	14,482.00	13,020.00
Drumright	10,366.40	10,858.00
Ottawa	17,753.40	17,784.32
Grabham	27,786.64	24,502.00
Total	$89,103.44	$84,694.47

Mr. Black's total was within 5 per cent of Mr. Truman's total on these items.

George Renner, of Topeka, an experienced estimator on building construction, testified (Tr. 2440) that he had checked the plans of the Ottawa and Grabham compressor stations estimated by Mr. Reintjes, and that if bidding on the work at Ottawa his bid would be $28,434, as against $45,019 by Mr. Reintjes. Both estimates have the heating and lighting eliminated, and at Grabham his bid would be $19,048 on the same items Mr. Reintjes estimated at $29,617.

Mr. Black introduced, as exhibit 53, photostats of the sworn returns, dated February 1, 1931, of the company on value for taxing purposes, to the Oklahoma Tax Commission. This report states that as at the date of that return the Hominy compressor station was being reclaimed, and that the Hogshooter compressing station, "is now and has been abandoned for several years. This property is now subject to sale and reclaim and has only a junk or salvage value of not to exceed $5,000." The Owassa station is twenty-five miles or more from any lines of the company; the equipment has been moved and the station is not in use.

Mr. Eastman testified (Tr. 2524) that during the last three or four, possibly five years, the Hogshooter station has not been operated due to the fact that the compressor station capacity was installed at the Tallant station. He [fol. 136] testified (Tr. 2524) that the company was refrain-

ing from using the Hogshooter station because of the necessity of repairing an 18-inch line extending north from that station so it will be capable of carrying high pressure.

In the reply brief counsel for the respondents suggest that the Commission should give no weight to the sworn affidavits before the Oklahoma Tax Commission, stating that these stations were no longer used and useful, because the company may have been over-zealous in its attempt to reduce taxes. We believe that these affidavits, in connection with the other testimony, clearly show that the stations are not at this time used and useful. We condemn he act on the part of the company by which they state, under oath, to one Commission that property is not used and useful for the purpose of defeating their obligations to the government, and make an opposite statement, under oath, to another Commission for the purpose of increasing their revenue at the expense of the general public.

This attempt on the part of the respondents in this case to add approximately a million dollars to the valuation by including compression stations properties in Oklahoma is an illustration of perverted corporate practice. Only a company drunk with power or saturated with arrogance would try to hoodwink a regulatory body in such manner. This Commission does not look with favor on such methods that would bolster a utility valuation in a rate case and at the same time avoid paying its fair share of tax revenue to the states.

In view of these facts we find that these three stations should be eliminated from consideration and we are deducting the value of buildings at these stations from the reproduction new and depreciated values, in arriving at our conclusions.

The company introduced, as exhibit 10, a report of per cent condition of this account as arrived at by inspection by P. McDonald Biddison, a consulting engineer of experience; J. H. Biddison, trained by P. McDonald Biddison; and F. D. Renfro, superintendent of compressor stations of the company. Mr. Eastman (Tr. 1312-1336) compared his own estimates of per cent condition of the property in this account with those of these three other experts, and showed that he had generally used a higher per cent condition than Mr. Biddison; in some cases Mr. Eastman used

a per cent condition 15 per cent higher than Mr. Biddison's, but ordinarily the difference ranged from 1 to 5 per cent.

Mr. Black also determined the per cent condition of the property in this account by inspection and found an average [fol. 137] condition 4½ per cent lower than that of Mr. Eastman's. Mr. Black's per cent condition appears ample in the light of the testimony of the company's experts.

After consideration of all evidence and exhibits, we find the reproduction cost new of this account to be $1,668,151, and the present fair value to be $1,466,102.

Account No. 1329

Transmission—Measuring Station Structures

This account includes all measuring structures, housing materials and regulating equipment, including town-border stations. The account is valued by Mr. Black at $147,337 new, and $133,310 depreciated. The account is detailed on pages 943 to 1145, 1731 to 1733 and 1861 to 1863. These structures were checked in the fields for size, were classified with respect to size and type and the price developed on the basis of detailed estimates of qualities for each class of structure, for the approximately 900 structures in the account. The company introduced exhibit 54 (Tr. 2045), showing alleged omissions from Mr. Black's valuation of 39 meter settings and housings, which should be classified under Accounts 1329 and 1332. No separation was made in exhibit 54 of these accounts and the amounts claimed have been added in Acocunt 1332.

Mr. Hamilton's exhibit 17 shows a total value of $165,893 new, and $155,018 depreciated for this account. No details were given as to the number of structures and no testimony was offered by any of the company's witnesses concerning such totals. We find the present fair value of this account to be $133,310.

Account No. 1330

Transmission—Other Structures

This account comprises small office buildings, barns, dwellings, storehouses, warehouses, garages and miscellaneous structures and improvements used in connection with the operation of the transmission system. The account is

valued by Mr. Black at $128,764 new, and $113,341 depreciated.

Mr. Hamilton values this account at $131,503 new and $118,604 depreciated.

We find the present fair value of this account to be $113,341.

[fol. 138] Account No. 1331

Transmission—Compressor-Station Equipment

This account covers all machinery and equipment used in connection with the operations of compressor stations. The account is valued by Mr. Black at $9,660,183 new and $8,482,419 depreciated.

A field check was made by Mr. Black of the items in this account from a detailed inventory furnished by the company, and costs of compressors and other equipment was determined by quotations from manufacturers.

Mr. Hamilton valued this account at $9,773,798 new and $8,873,812 depreciated.

Both Mr. Black and Mr. Eastman fixed the per cent condition of the property in this account by inspection. The company introduced exhibit 10 to show the per cent condition observed by P. McDonald Biddison and Mr. Renfro, who also observed the per cent condition of compressing station structures. Mr. Eastman did not use the observed condition per cent fixed by Mr. Biddison and Mr. Renfro, but applied a somewhat higher per cent. He testified (Tr. 1341-1345) to applying 85 per cent condition to main compressor units to which Mr. Biddison and Mr. Renfro applied 80 per cent; he applied 95 per cent condition to auxiliary equipment to which Mr. Biddison and Mr. Renfro applied 85 per cent; he used 85 per cent on machine shop equipment to which Mr. Biddison and Mr. Renfro applied 70 per cent; he applied 85 per cent condition to miscellaneous equipment at Tallant station to which Mr. Biddison and Mr. Renfro applied 75 per cent.

It therefore appears that the fact that Mr. Black's per cent condition on this account is 3 per cent less than that of Mr. Eastman is not out of line when compared with the per cent condition fixed by Biddison and Renfro.

Attention was directed in our discussion of Account 1328, Transmission—Compressing Station Structures, to our conclusions omitting the Owassa, Hominy and Hogshooter stations, because they are neither used nor useful and we have eliminated from this account $705,957, for the reproduction cost new and $433,509 for the present fair value of equipment in these three stations.

We find the reproduction cost new of this account to be $8,954,226 and the present fair value to be $8,048,910.

[fol. 139] Account No. 1332

Transmission—Measuring-Station Equipment

This account includes measuring station equipment, regulators and pipe fittings entering into the installation thereof, dust separators and other miscellaneous equipment used for measuring gas. These items were checked in the field and prices applied in accordance with quotations received from manufacturers in the case of equipment, and developed prices applied to those structural items on which it was necessary to make calculations.

This account is valued by Mr. Hamilton at $1,174,804 new, and $1,143,231 depreciated.

Regulators and meter settings in Kansas are carried in Mr. Hamilton's appraisal at $599,993, without explanation; regulators and meter settings are carried in Missouri at $99,033 and the same item is carried for Oklahoma at $156,487. Testimony in connection with these lump-sum items was given by Mr. Eastman (Tr. 1331) to the effect that meter and regulator statistics were too voluminous to include in detail in his report.

The company introduced exhibit 54 (Tr. 2045), showing 39 meter settings and housings had been omitted by Mr. Black from Accounts 1329 and 1332. Exhibit 54 does not allocate these items between Accounts 1329 and 1332 and so the entire amount is added to Account 1322 in the amount of $25,100 to reproduction new, and $24,006 depreciated.

With the exception of the items listed in Exhibit 54, the company gives no detail of this account. Mr. Black's items were segregated, and in such detail the company was able to detect the omission of thirty-nine stations, the reproduction cost of which was $25,100. Mr. Hamilton arrived at this account in Kansas in a lump sum of $599,993 (Tr. 1351).

In our opinion the totals arrived at by Mr. Black for cost of reproduction new and depreciated are fair when the amounts noted above for thirty-nine stations are added. We find the present fair value of this account to be $759,625.

Account No. 1333

Transmission-Line Equipment

Transmission-line equipment includes the largest item of value in any account. Mr. Hamilton's cost of reproduction new being $46,893,014 and cost of reproduction new less [fol. 140] depreciation $43,578,602, while Mr. Black's cost of reproduction new was $43,099,711, and cost of reproduction new less depreciation $38,842,371.

There were many points of difference between Mr. Black and Mr. Hamilton as to many of the items entering into this account and a great volume of testimony and many exhibits were introduced relating to this account.

As we have said in connection with our discussion of production field line equipment, Account No. 1314, we shall discuss the later account and the transmission-line equipment account together, because both of these accounts include common items of cost of construction, labor and material.

Mr. Black's exhibit 42 consists of 440 pages of the detailed development of direct, overhead and unit prices of pipe and other materials entering into the construction of this property. Pages 1 and 2 of this exhibit is an analysis of the direct structural overhead in Kansas for labor and materials, showing the amounts, in per cent, allowed for omissions and contingencies, purchasing, stores, expense, supervision and inspection, workmen's compensation, public liability, tool expenses, miscellaneous construction expense, performance bond and contractor's profit. Similar analyses are given for Missouri, Oklahoma, Nebraska and Texas.

Page 11 is a development of labor cost for the installation of pipe fittings and valves. Pages 14 to 17, inclusive, develop the cost of pipe of all kinds, delivered for each of the five states in which the gas company has lines. This pipe cost development shows size and kind of pipe, weight per foot, and the cost per foot, including overheads, delivered in Kansas, Oklahoma, Texas, Missouri and Nebraska. On

pages 18 to 25 there is developed labor costs for the unloading, hauling, stringing, ditching and laying of these lines. Pages 24 to 440 develop the cost, installed, of valves, fittings and other items entering into the construction of the system. In the case of general building construction, and in cases where materials or labor prices are not covered by exhibit 42, and where the prices developed in the exhibit required further explanation or breakdown, or where further explanation or breakdown was requested, it was given by Mr. Black in the detail desired.

Contrasted with this exhibit 42 and the testimony of Mr. Black on the development of labor and materials costs is the testimony of Mr. H. L. Eastman, testifying in support of Mr. Hamilton's valuation exhibit, and the unit cost used therein. The only exhibits showing development of unit costs used in Mr. Hamilton's exhibits were introduced by [fol. 141] Mr. Black as exhibits 73 and 74, covering data received by Br. Black from Mr. Eastman.

Mr. Eastman, testifying on the breakdown of labor prices used in Mr. Hamilton's exhibit for unloading, hauling, stringing, ditching, laying pipe and backfilling the ditch, said he had no breakdown of such prices, or of the supporting data back of them, other than analyses his company had made of actual construction costs during the period dating back to 1924. He was in all cases unable to testify concerning the data underlying the figures used, excepting that it was too voluminous to produce in court. His testimony with respect to development of "pick rock" and "shoot rock" prices was the same. This underlying data was developed according to Mr. Eastman by putting men out on construction jobs and analyzing the contractor's costs of each operation.

The contract cost for pipe-line construction, as shown by the construction contracts under which much of the pipe-line system of these companies has been constructed, is usually on the basis of one unit price per foot for unloading the pipe, hauling, stringing, ditching, in all classes of excavation, laying the pipe and backfilling. It is apparent that when such construction operations are analyzed in accordance with Mr. Eastman's testimony, and the costs so developed are applied to units of work done, and the total so arrived at is compared with the contract cost by a reputable contractor for the same operations, there should

be some reasonable relation between the two, but the record in this case does not indicate any such relation. Mr. Black's exhibit 77 compares the contract costs of unloading pipe and materials, hauling, stringing, ditching in all classes of materials, laying pipe, backfilling and testing on seven of the lines in this property with the amounts claimed in Mr. Hamilton's exhibit for "pick rock" and "shoot rock" only. Line "G" between Wichita and Ottawa, cost the company $0.59 per foot for all the above operations, including rock excavation, under a contract dated June 22, 1928, or a total of $379,699. Mr. Hamilton's valuation, based on an analysis of costs of contract operations, shows the cost of rock excavation only to be $390,276, or $10,577 more than the contract cost of all operations for the construction of this line excepting welding and painting. Mr. Eastman testified that Mr. Hamilton's classification of earth, shoot rock and pick rock in the pipe lines of the system was determined by engineers sent over the lines for that purpose. Mr. Eastman testified that where any shoot rock was shown in the valuation it had been calculated as solid from top to bottom [fol. 142] of the trench, and that where any pick rock was shown the entire excavation had been calculated as pick rock.

It is difficult to imagine a condition where a contractor would make a competitive bid on rock excavation, or where a company would pay for rock quantities excavated, on any such basis, particularly when the unit price for shoot rock has been developed by Eastman at $7.38 per cubic yard, and pick rock at $4.01 per cubic yard. It is a matter of common knowledge that rock, both solid and loose, may be found from top to bottom in trenches, or it may carry an overburden of earth and only a few inches of rock show in the lower part of the pipe-line ditch. The matter of calculation of such excavation, where paid for by unit prices for earth and for rock, may readily become a matter of argument between the contractor and the company. In the case of Line "G" between Wichita and Ottawa, the company contracted with Mr. Jones, a pipe-line contractor of fourteen years' experience who has in that period constructed pipe lines involving the expenditure of about $20,000,000 for labor, to unload, haul, string and lay the pipe, excavate the ditches, including shoot rock and pick rock, backfill and test the line, for $0.59 per running foot. It is presumed that before making any such bid the contractor

informed himself concerning the kind of excavation he would likely encounter in the 130 miles of line; he testified that he received a total of $895,985.67 for this contract and that he lost $128,000 on it, but he did not allocate any part of this loss to pipe unloading, hauling, stringing, ditching, backfilling, or to the other operations for which he received unit payments in addition to the $0.59 per foot, and which amounted to $516,287 in addition to the $379,699 paid for the operations included in the $0.59 per foot bid. Mr. Jones testified that the reasonable cost per lineal foot for excavating solid rock would be "a little over 75 cents" in a ditch 28 inches by 40 inches. Such a ditch contains 7.8 cubic feet of excavation per lineal foot of ditch, and the cost of solid-rock excavation per cubic foot may then be taken as 9.62 cents. Mr. Jones' reasonable cost for excavation of solid rock in a ditch of this kind then becomes 27 times 9.62 cents or $2.60 per cubic yard. This price compares with Mr. Eastman's price of $7.38 per cubic yard for shoot-rock excavation, and his price of $4.01 per cubic yard for pick-rock excavation. Mr. Jones' testimony concerning reasonable costs for solid-rock excavation was made after the completion of this contract.

Mr. Black's testimony with respect to classified excavation was that he determined the percentage of such excava- [fol. 143] tion by observation of the territory through which the major part of these lines passed, and from his knowledge of the territory gained through more than twenty years' experience; he testified that he made a personal inspection of Line "G" from Wichita to Ottawa, and that he had allowed $2.50 per cubic yard for all classified excavation, whether solid or loose rock, and had allowed this amount in addition to ordinary cost of trenching and backfilling of ditches of the same dimensions. This average allowance of Mr. Black's for solid and loose rock is ample when considered with Mr. Jones' testimony of $2.60 per cubic yard for solid-rock excavation only.

If we assume that Mr. Eastman's classification of shoot-rock and pick-rock excavation is correct, it appears that he has used 2.8 times as much as he would have used for shoot-rock excavation on the basis of Mr. Jones' cost, and 2.9 times Mr. Black's cost. His allowance for pick-rock excavation cannot be compared with Mr. Jones' development for cost of solid-rock excavation excepting in so far as it

is $1.41 per cubic yard in excess of the allowance Mr. Jones made for solid-rock excavation. It is also $1.51 per cubic yard in excess of Mr. Black's allowance for both shoot and pick rock. In view of this apparent discrepancy between the developed prices of Mr. Eastman for rock excavation, and the reasonable prices testified to by Mr. Jones, and the prices developed by Mr. Black out of experience and rock excavation costs on contracts supervised by him in Oklahoma, Kansas and Missouri, we think but one logical conclusion can be drawn and that is to adopt the prices developed by Mr. Black.

Mr. Eastman compared labor costs to the company with labor costs used by Mr. Hamilton in exhibit 17, and by Mr. Black in exhibit 41, on eleven major pipe lines, as shown by the following tabulation:

Line	Company Labor	Hamilton		Black
		Labor	Labor and Couplings	Labor and Couplings
Hutchinson-Superior	$355,893	$382,744	$429,343	$348,436
Fort Scott 8"	202,184	180,961	194,736	139,639
Springfield 10"	380,394	442,570	489,809	343,085
St. Joseph 12"	144,683	164,621	190,224	157,268
Quapaw 16" (new)	52,809	43,147	51,841	53,842
St. Joseph 16" (new)	62,244	48,746	53,582	43,803
Southern Trunk 16" (new)	95,548	95,622	111,172	86,459
Topeka 16"	180,345	166,415	192,177	144,869
Dilworth-Wellington	174,894	162,915	176,595	163,799
Ottawa-Law. Jct. 20"	175,005	151,602	177,072	142,050
Pampa-Wichita 20"	1,547,013	1,832,822	2,210,633	2,052,519
Total	$3,371,012	$3,672,165	$4,277,184	$3,675,769

To make the company's total for the eleven lines comparable with Mr. Black's total, we have arrived at the cost of couplings and welds in these lines by deducting Mr. Ham- [fol. 144] ilton's allowance for labor of $3,672,165 from his allowance for labor, couplings and welds of $4,277,184, giving $605,019 for couplings and welds; adding this to the company total labor of $3,371,012, we have $3,976,031 as the company labor total, including couplings and welds, and the comparable totals become:

Company labor costs plus—	
Hamilton's couplings and welds	$3,976,031
Hamilton—labor cost, including couplings and welds	4,277,184
Black, labor cost, including couplings and welds	3,675,769

Mr. Hamilton's valuation was therefore $301,153 more than the cost to the company when including $605,019 al-

lowed by Mr. Hamilton for couplings and welds, or 7.57 per cent above the company cost. Mr. Black's total allowance for the same items was $300,265 less than the cost to the company when including in the company total the $605,019 allowed by Mr. Hamilton for couplings and welds, or 7.55 per cent less than the company cost.

These comparisons would have been very materially changed had the tabulation included other major lines, or even one major line, such as line G, from Wichita to Ottawa, and which was constructed later than the Pampa-Wichita line included by Mr. Hamilton in the tabulation. The following tabulation shows this addition:

	Company	Hamilton	Black
Total of eleven lines	$3,976,034	$4,277,184	$3,675,769
Line G	895,986	*	1,088,341
	$4,872,020	.....	$4,684,110

* Totals not available.

On this basis Mr. Black's value is $187,910.00 or 3.86 per cent less than the company cost, instead of 7.55 per cent on the basis of the eleven lines tabulated by Mr. Hamilton. It is, therefore, apparent comparisons of parts of accounts do not truly reflect the differences in these valuations, for the result will vary in accordance with the lines selected. The only proper comparison is on the totals of these accounts, which are shown in the following tabulation:

		Hamilton		Black
Total of account 1314	.....	$4,447,806	.....	$3,548,102
Total of account 1333	.....	46,893,014	.....	43,099,711
Total both accounts	.....	$51,340,820	.....	$46,647,813
Deduct pipe	$28,684,477	.....	$27,333,912	.....
Deduct classified excava.	3,890,281	.....	1,270,115	.....
		32,574,758		28,604,027
Totals remaining	.....	$18,766,062	.....	$18,043,786

This tabulation shows that Mr. Hamilton's valuations for both of these accounts covering all labor and materials, exclusive of pipe and classified excavation, was $722,276 in excess of Mr. Black's valuation. Mr. Hamilton's labor [fol. 145] and coupling costs on the eleven major lines tabulated by him exceeded company labor and coupling costs 7.57 per cent, and on the totals of accounts 1314 and 1333, as shown by the above comparison, exceed Mr. Black's valuation 4 per cent; if Mr. Hamilton's excess of 7.57 per cent,

developed on the eleven major lines, is a fair measure of his excess over company cost on the labor in these two accounts, 1314 and 1333; it may also be argued that Mr. Black's valuation for these two accounts is 3.57 per cent higher than cost to the company, if such costs were comparable to the period in which these eleven major lines were constructed. However, we do not think these eleven lines were constructed in a period when material prices were comparable to 1931 prices, and for that reason we are of the opinion Mr. Hamilton's general labor and materials costs are excessive.

The major items of difference in the valuations of these two accounts, 1314 and 1333, are in classified excavation and in pipe. The testimony of the company's witness, Mr. Jones, taken in connection with that of Mr. Black, is conclusive with respect to the fair price of rock excavation. Mr. Black allowed a total of 508,046 cubic yards of rock excavation in these two accounts; Mr. Hamilton, estimated 514,468 cubic yards of pick rock and 247,596 cubic yards of shoot rock. Mr. Eastman's testimony that wherever encountered, pick rock and shoot rock were calculated from top to bottom of the ditch, as well as the effect of such computations when applied to line "G" (Black's exhibit 77), leads us to the conclusion that little if any weight should be given either his calculations of quantities of rock, or the price per cubic yard developed by him and applied to those quantities. We are of the opinion that Mr. Black has made an ample allowance for rock excavation in both Accounts 1314 and 1333.

As heretofore stated, one of the major differences in Accounts 1314 and 1333 is the allowance for pipe used in field and transmission lines. Considerable testimony was given concerning the base price of pipe, delivered prices of pipe, difference in prices of standard plain-end gas-line pipe, seamless pipe, screw pipe, electric-weld pipe, pipe of twenty-foot lengths, thirty-foot lengths and forty-foot lengths, and pipe with double bell ends. Testimony was offered also concerning the effect of freight rates to various points in the territory covered by the transmission system of the company, and also to show that the price of pipe at any given point was competitive; or, in other words, that whether shipped to Oklahoma City from Chicago or Lorain, it would have the same price per foot at Oklahoma City.

[fol. 146] This means the mill price of the pipe would vary, for, obviously, the freight from mill to point of delivery would remain constant for a given point.

Mr. Hamilton's pipe prices are all based on pipe from the Chicago district delivered f. o. b. Cambridge, Kan., on the assumption that freight from the Chicago district to Cambridge would be the average freight cost for all points on the system. Mr. Black's pipe prices are predicted on shipments from Lorain with freight added to point of delivery. Mr. Black's testimony is that the freight rate of 84 cents per 100 pounds from Lorain to Cambridge, Kan., is the same as it is to all points on company lines south of Cambridge in Oklahoma, and to points southwest in Texas on the lines of this company; that the Lorain rate is 61½ cents per hundred pounds in the Kansas City district; that it is somewhat higher at points along the lines of the company in northern Kansas and Nebraska. He, therefore, made a weighted average freight rate from Lorain for the entire state of Kansas, by applying the rates at various points to which pipe would be shipped to the weight of pipe which would be delivered at such points and arrived at a weighted rate for the state of 77 cents per 100 pounds. Nebraska was divided into two districts because of the variation of rates in the Superior district and Falls City district, and average rates were applied to pipe within those districts. Missouri was divided into two districts, one being the northern part of the state and the other the southwestern portion, and the average freight rate for each district was applied to pipe delivered therein. The difference between these weighted freight rates and the Lorain-Cambridge freight rate is $387,246. In other words, pipe in the system shipped from Lorain to Cambridge as a central point costs $387,246 more for freight than if shipped to the points at which used, at the freight rates applying to those points. Obviously the pipe was not shipped Cambridge but to the rail points nearest the point of use. If pipe prices are competitive at a given point, regardless of its point of origin, and the testimony is to that effect, it seems clear that by Mr. Hamilton's method of considering Cambridge the common point of delivery he has overpriced the pipe in his valuation by $367,246. The freight rates from the Chicago district to Cambridge were 58½ cents per 100 pounds, 69 cents to Amarillo and points

on the Tampa-Wichita line, 64½ cents to Oklahoma City, 35 to 43½ cents at Missouri points, 58½ to 77 cents at Kansas points and 35 to 61½ cents at Nebraska points.

In order to arrive at the true difference between pipe [fol. 147] prices in Mr. Hamilton's valuation and his own by calculating the pipe at a common delivery point, Mr. Black introduced exhibit 83, which is a summary of pipe in all gathered and transmission lines of the company, classified with respect to kind of pipe, total footage, total weight and total costs f. o. b. Cambridge, Kan., at Hamilton's prices and at Black's prices. This summary shows Mr. Hamilton's allowance for pipe f. o. b. Cambridge, Kan., totaled $27,318,551, while Mr. Black's allowance on the same quantity of pipe at Cambridge was $26,773,999, a difference of $544,552. This difference amounts to $1.51 per ton. The testimony developed the fact that this difference in price per ton appeared to be a reasonable difference in pipe prices, particularly when one considered the basis on which these prices were obtained by the company; that is, letters to the manufacturers of pipe asking them to quote on the delivery of approximately 359,700 tons of pipe of various kinds in the system.

There was some difference of opinion as between Mr. Hamilton and Mr. Black as to the cost of some pipe, especially screw pipe. The testimony was to the effect that plain end pipe cost less to buy and to lay and was less subject to leakage and depreciation than screw pipe. It appears that screw pipe costs more than plain end because the former has become obsolete, is not generally used and is not readily available. While screw pipe should be subject to depreciation to cover these factors we are not making any deduction therefor in the absence of any testimony as to the extent of such deductions. We find that the cost of pipe is $27,318,551 as included by Mr. Hamilton in his appraisal which is the price f. o. b. Cambridge, from which should be deducted $387,246 for excess freight included by Mr. Hamilton when he considered Cambridge, Kan., as a central shipping point instead of calculating freight to actual point of destination where pipe would be unloaded, which results in an allowance for this material of $26,931,305.

Exhibits 4, 5, 6, 7 and 20, all dealing with present conditions of pipe lines in Account 1333, were introduced by

the company. Exhibit 4 is a map showing the pipe-line system of the company, on which was indicated the location of various inspections. Mr. Hamilton referred to a total number of 17,700 inspections of the pipe lines of the company. Mr. Hancock testified 17,746 inspections had been made on the property and that this meant an average of one inspection for each 1,300 feet of pipe line. He also testified that 16,330 of these inspections had been made in the routine maintenance work of the company. On cross-[fol. 148] examination Mr. Harcock testified that 7,130 of these inspections had been made on the St. Joseph 16-inch line in a length of approximately 200 miles; that 6,667 of these inspections had been made in the approximately 50-mile length of line between Garnett and Ottawa, Kan., and furthermore, 6,667 of these inspections were made in 1927, and that the additional four years' life between 1927 and 1931 meant nothing when considering the present per cent condition of the line, because the added four years of depreciation would not be ascertainable by inspection. From this testimony it appears clearly that these 13,797 inspections made on approximately 250 miles of pipe line should not be seriously considered in a general average of inspections over the entire system, and should be given weight only on that section of the line on which they were made.

Mr. Hamilton testified that 506 inspections were made by engineers for the company accompanied by engineers for the Commission and that 822 additional openings were made by the engineers for the valuation department. Mr. Biddison testified that he made 142 inspections and that he thinks he reached a fair conclusion as to the system as a whole by these 142 inspections. In response to cross-examination he testified that the per cent condition applied to certain lines in the system did not reflect his judgment, inasmuch as the per cent condition applied by engineers for the company were different than those arrived at by him.

Mr. P. J. Richards testified to having analyzed 101 soil samples taken along the lines of the company, and having determined that 2 per cent of the line would last two to six years, 2 per cent six to twelve years, 12 per cent less than twenty years, and the remaining 84 per cent would last fifty years. He also testified that he could not determine the per cent condition of pipe by his method, but that he

could and did determine the life expectancy by a comparison of analyses of soils along the lines of the gas company's system, with the analysis of a soil in which the Bureau of Standards had buried pipe and which pipe was removed from time to time and the effect of the soil noted. He testified that his calculation was based on bare pipe. Most of the pipe in the system is either wrapped or painted and Richard's calculation on bare pipe would not be applicable. He had made no calculation on the per cent condition of the property.

Prof. A. M. Ockerblad testified with respect to laboratory tests he had made on coupons cut from pipe lines in the [fol. 149] transmission system of the company, in order to determine the tensile strength of the pipe. Inasmuch as there is no contention on the part of the state that inferior pipe has been used in the construction of this system, and no claim has been made that the system was overbuilt with respect to heavier pipe than was required, nothing will be gained by discussing Professor Ockerblad's tests.

Engineers from Mr. Black's office accompanied the engineers for the Cities Service Gas Company on an inspection of 506 inspection pits scattered over the entire pipe-line system. These inspections and Mr. Black's calculations were not weighted with the 16,330 inspections made by the company in the maintenance work on the system.

After considering the testimony of witnesses in respect to present conditions of the pipe lines, we are of the opinion that a condition of 90.1 per cent as testified to by Mr. Black apparently represents the average condition and have adopted that percentage.

It appears that Mr. Black had originally included in his valuation an item of $82,976 for paint on the Pama-Wichita line. This item was omitted by Mr. Hamilton, and Mr. Black's valuation corrected accordingly. However, it later appeared that Mr. Hamilton's omission was incorrect and that this item should be included and added to Mr. Black's value.

After giving consideration to all of the testimony and the exhibits relating to Transmission Line Equipment, Account No. 1333, we find that the reproduction cost new of this equipment was $43,746,298 and that the reproduction cost new less depreciation was $39,422,331.

Account No. 1334

Transmission—Other Equipment

This account is valued by Mr. Black at $6,938 new, and $5,633 depreciated. The account consists of water wells, tanks, and pumping equipment and station-lighting equipment at Cutton Valley, Drumright, Oklahoma City and the Seminole 16-inch junction in Seminole county.

This account is valued by Mr. Hamilton at $8,334 new, and $6,835 depreciated.

We find the present fair value of this account to be $5,633.

[fol. 150] Account No. 1379

General—Other Structures

In general, the account covers dwelling, garages, office building, warehouses and miscellaneous structures not classified under Accounts 1310, 1311, 1328 and 1330.

This account is valued at $117,396 new and $94,687 depreciated and we find the present fair value of this account to be $94,687.

Account No. 1384

General—Garage Equipment

This account covers all autos, trucks, trailers, garages, tools and equipment owned by the company. The account is valued by Mr. Black at $174,139 new and $74,481 depreciated.

The inventory of the company for this account was accepted by Black. Automobiles, trucks and similar equipment was priced by him but other equipment prices fixed by the company were accepted by Black.

This equipment is valued by Mr. Hamilton at $164,391 new, and $81,448 depreciated.

Mr. Black reaches a value new of $9,748 in excess of Mr. Hamilton's value. The difference is accounted for by the fact that Mr. Black priced the automobiles and trucks included in this account through dealers, without having knowledge of the special discount available to the Cities Service Gas Company in purchasing such equipment, while

Mr. Hamilton gave consideration to such discounts. We feel that it cannot be disputed, therefore, that the valuation found by Mr. Hamilton reflects more accurately what it would actually cost the company to reproduce these cars. Mr. Black found a depreciated value of $6,962 less than that of Mr. Hamilton. Without weighing the merits of the manner of arriving at the depreciated condition, but considering the fact that Mr. Hamilton used special discount figures in arriving at his cost new, we find that his depreciated cost of $81,448 should be used in the valuation as the present fair value of this account.

Account No. 1386

General—Telephone and Telegraph System

This account covers telephone and telegraph lines used by the gas transmission system of the Cities Service Company. The account is valued by Mr. Black at $480,641 new [fol. 151] and $410,999 depreciated. Mr. Hamilton's value is $535,493 new and $486,182 depreciated.

The inventory supplied by the company was accepted by Mr. Black as correct without check. The account was priced by quotations from manufacturers for materials, and installation costs were calculated by Mr. Black.

The company questioned the value priced on two towers at the crossing of the Arkansas river and introduced exhibits 55 and 56, showing that the actual cost of these towers and foundations in 1927 was $5,000. Because of lack of time Mr. Black did not make an inspection of these towers and the values were fixed on the description furnished by the company. Apparently, the value on this account should be increased by $4,285 to take care of the difference in the reproduction cost new of this item. Depreciating this added amount at the rate used by Mr. Hamilton gives $4,071 as the amount to be added to Mr. Black's present fair value of $410,999.

We find the present fair value of this account to be $415,070.

Engineering and Superintendence

Valuation witnesses for both the company and the Commission estimated engineering and superintendence during

construction at an amount equal to five per cent of physical property after excluding certain general accounts which would not require engineering.

Mr. Black testified that his allowance for engineering and superintendence was intended to cover all details of supervision and engineering in the location of pipe lines, preparation of plans and specifications, general engineering and supervision of construction, preparation of estimates, inspection and testing of materials and equipment, except some inspection and testing of pipe for which he had made allowances otherwise, and all other work usually carried on by an engineering organization on construction projects.

Mr. Hamilton stated that his estimate included engineering and superintendence of design, supervision of construction from an engineering standpoint, including superintendence as to the feasibility of the project, determination of quantities of gas to be delivered, size of pipe necessary, amount of production necessary to handle the load, determination of location, the compressor stations required and engineering in testing equipment after installed. He testified he arrived at his estimate of engineering and superintendence by applying 5 per cent to physical property values as he had estimated them.

[fol. 152] In view of the testimony of both witnesses that engineering and superintendence should be estimated at an amount equal to 5 per cent of physical property except certain items of general equipment, we find that allowance for engineering and superintendence during construction should be based on five per cent of physical property valuation excepting as to Accounts 1316, 1380, 1381, 1382, 1383, 1384, 1385, 1387 and 1388, which would require no engineering. We find the cost new to be $3,218,585, and the depreciated value to be $2,881,000.

Taxes During Construction

Mr. Hamilton computed taxes during construction at $769,174, which he estimated based on 1 per cent of the physical property and on a construction period of two years, and did not depreciate such allowance.

Mr. Black estimated taxes during construction by finding the amount of taxes actually paid by the company for one year and converting the tax payment into percentage of

total depreciated cost of reproduction and used that percentage in estimating taxes during the construction period. This percentage was applied to a two-year construction period and we have adopted Mr. Black's estimate based on the actual experience of the company, which results in an allowance of $875,171, in the cost of reproduction new and $778,044 in reproduction cost new less depreciation.

Interest During Construction

Mr. Hamilton allowed $6,337,386 for interest during construction, which he does not depreciate, and he testified that it was based upon an allowance of 8 per cent on a two-year construction period, "and put it in at 8 per cent for one year." That is, he used a two-year construction period and allowed 8 per cent return on the investment during half the time on all of the property. He assumed that for the first two years during which the property was being constructed there would be no income.

Mr. Black's estimate of interest during construction was based on a two-year construction period at the rate of 6 per cent. He assumed that land and right of way would be acquired early in the construction period and allowed two years' interest, or a total of 12 per cent on land and right of way. He allowed interest during construction on all property plus engineering and superintendence, administration and legal expense and taxes during construction. He assumed that part of the system would be placed in operation [fol. 153] before the entire project was completed. He did not make any allowance for interest on bank balances during construction.

The evidence shows that six per cent is the rate which the company has actually paid on borrowed money other than bonds. On page 43 of their reply brief, respondents contend that the investor is entitled to the same return on his money during the period the plant is being constructed as he is allowed to receive after the project is placed in operation. "You have the same investor and the same money going into the project. Whatever is fair in one case must be in the other." This theory is not sound.

There is little relation to be found between a rate of interest to be allowed for the use of money borrowed or ad-

vanced in construction, and a rate of return on the value of property when subsequently put into public service. The latter involves the continuance of operation, and many other considerations. An examination of the decisions will disclose that interest during construction is never measured by the rate of return allowed. We find that an allowance for interest during construction based upon an interest rate of 6 per cent is reasonable and that an allowance should be made of $4,351,934 in cost of reproduction new and $3,883,282 in the cost of reproduction new less depreciation.

Cost of Financing

Mr. Hamilton included in his valuation an item for cost of financing of $3,422,512 undepreciated. Mr. Hamilton stated that this estimate was based on 4 per cent of the total value including interest during construction. He further testified that the company would be put to no expense in selling securities to the Cities Service Company, but that he based his estimate on the value attributable to its ability to so place its securities without expense.

Mr. Hamilton's theory is that this company would come here without any capital and without credit, and that it would have to go out into the markets and entail great expenses in convincing somebody that had money that this would be a profitable enterprise, and that the company should be entitled not only to a fair return on the actual investment necessary, but would also be entitled to a return on the expense to which it would be put because of its improvident and impoverished condition.

Mr. Black made no allowance for cost of financing in his valuation, and we think properly so. This company is en- [fol. 154] titled to a fair return on the capital which it prudently invests in the enterprise and no more.

We are attempting to find present value, and we must assume a construction by persons financially able to construct. Otherwise, the more impecunious the organizers, and the more subject to excessive cost of procuring money, the greater would be the present value of the property. This matter has been disposed of in recent decisions.

In Minneapolis v. Rand (285 Fed. 818, 829) the United States circuit court of appeals said:

"The cost of financing is assumed upon the theory that a company, desirous of establishing such a plant, should not be possessed of sufficient capital to pay for the plant and should be compelled to borrow money by floating securities through brokers and should be exposed to large discounts if compelled to obtain money in this way. The fair value of the plant should not be estimated upon such a basis of impecuniosity and exactions, but upon the theory if used, of reconstruction, by those financially able to build the plant, paying reasonable prices therefor."

In Colorado Power v. Halderman (295 Fed. 178, 191) United States District Judge Symes said:

"A valuation is also claimed for marketing of securities. This is not a proper item."

We disallow the claim in its entirety.

Working Capital

Mr. Hamilton estimated working capital requirements at $772,126, which he testified was equal to two months' operating expenses and one month's gas purchases.

Mr. Black based his estimate of working capital on one and one-half months' expenses, including cost of gas based on an annual outlay of $6,200,000, arriving at the round sum of $775,000 which we find to be reasonable.

Material and Supplies

Mr. Hamilton used $548,096 for materials and supplies requirements based on the materials and supplies on hand September 1, 1931, according to the books.

Mr. Black used the average cost of materials and supplies on hand according to the books at June and September 1, 1931, of $509,400.

Respondents contend that $119,275 should be added to Mr. Black's valuation because of alleged omissions by him [fol. 155] of compressor station spare parts. Mr. Hamilton's testimony throws some light on this subject:

"Q. Materials and supplies, that is $548,096. What is that?

A. Oh, it is the warehouse materials that are carried on hand. It is pipe and fittings and compressor station repair parts, and various items of that nature."

Mr. Black's testimony was that his allowance of $509,400 for materials and supplies, was the average of the June 1, and September 1, accounts furnished him by the Commission's accounting department, and that if these items were included in materials and supplies on hand on the books of the company they are included in his valuation. There is nothing in the record to show Mr. Hamilton's allowance of $548,096 did not include these spare parts, his testimony is that it did so include them; Black properly used an average of the account on hand at two different dates, and this accounts for the difference between the allowances by Hamilton and Black. We believe that an average cost is more representative of average conditions than the cost for one day and that if Mr. Hamilton's value was so averaged it would approximate the value reached by Mr. Black. We find that $509,400 is a reasonable allowance for materials and supplies.

Intangible Values

Although, perhaps, not strictly intangible as that term is restricted in valuation proceedings, the following are items not associated in either valuation submitted with the acual physical materials and structures:

Organization.
Administration and legal expenses.
Miscellaneous construction expenses.
Going value.

These items are more or less elusive, and the witnesses based their estimates mainly on percentages of other values. The allowances undepreciated included in the respective valuations follow:

	Black	Hamilton
Organization	$482,754	$384,586
Administration and legal	1,287,348	384,586
Miscellaneous construction expenditures	.....	769,174
Going value	3,820,000	8,898,532
Total	$5,590,102	$10,436,878

These items will be discussed in the above order.

[fol. 156] Organization Expenses.

Mr. Black included in his estimate of value an item of organization expense equal to three-fourths of one per

cent of physical property value to cover preliminary organization and legal expenses, preliminary engineering and geological expense, organization expenses up to time construction begins, preliminary survey and market survey.

Mr. Hamilton included organization expenses at one-half of one per cent of physical items, including preliminary work of getting the organization together, incorporation expenses other than legal expenses, "and items of that nature," and he could not itemize and assign costs to any of the items.

We find an allowance for organization should be based three-fourths of one per cent of the physical value giving a cost new of $480,008, and the value is not depreciated.

Legal and Administration Expense During Construction.

Mr. Hamilton, witness for the company, estimated law expense during construction at the rate of one-half of one per cent of physical property and included legal expenses for incorporation, drawing of contracts and the type of work that must be done prior to and during the construction of the property, charter fees, tax stamps, and expenses that had to do with the issuance of securities. He stated that he was unable to break down this estimate and, "I have never been able to, one of these legal fees."

Mr. Hamilton did not have the history of the actual legal expenses incurred during the construction of the plant, but testified that they would be incurred in drawing contracts, damage claims and items of that kind.

Mr. Black's estimate of legal expenses was combined with an estimate of administration expenses during construction, and he estimated the aggregate of both at two per cent of the physical property. He tesified that the organization and legal expense covered the cost during the construction period of administering the general business of the company, including mainly administration and legal expense and part of the organization that eventually becomes a part of the operating organization of the company.

Mr. Hamilton did not depreciate legal expenses; Mr. Black depreciated his estimates based on cost to reproduce new. We find an allowance for legal expense during construction should be based one-half of one per cent of the

[fol. 157] physical values, including engineering, giving a cost new of $340,094 and a depreciated value of $304,084.

Miscellaneous Construction Expenditures.

Mr. Hamilton included $769,174 for miscellaneous construction expenditures consisting of office rent, office employees and "various disappearing items of that nature during the construction period," arriving at the amount by applying one per cent to physical property.

Mr. Black included such items in other accounts.

In view of the fact that Mr. Black included such items in other accounts, a great number of which has been adopted in this valuation, it is doubtful whether or not an allowance should be here made. We are, however, for the purpose of taking care of any miscellaneous expenditures, allowing 1 per cent of the physical values including engineering and find that the reasonable value is $680,187 for the cost new, and $608,169, as the depreciated value.

Going Value.

Going value is that uncertain and elusive item of additional value which it is said inheres in an "assembled and established plant, doing business and earning money, over one not thus advanced." That is, the material and labor entering into the construction of a public utility property has so much value as so many units of material and so many hours of labor. When, however, the material and labor become part of a completed going property they take on a new value, which is not only the aggregate of the cost of the material and labor, but is the value of a property as it exists in use and with its business established, as distinguished from a bare aggregation of units of property. This additional value does not include "good will" as good will is generally defined, nor is it a value based upon capitalized earnings or a capitalization of pioneer losses or past operating deficits.

Going value may be defined, we think, as "that amount by which the value of a utility plant in operation, with customers attached and an established revenue, exceeds the value of an exactly similar plant all ready to go, or going, without any customers or revenue, but so situated that the

acquisition of customers and revenues is a mere matter of time and ordinary adjustments."

The best measure of the going value is to be found in the cost of creating such going value. The cost would include such intangible values as organization and legal expense, [fol. 158] administration costs during construction, cost of training employees, cost of records, cost of attaching business, and possibly some allowance for interest during construction and on idle plant. The items of interest and depreciation might properly be omitted from consideration because an allowance for interest and depreciation on idle plant is simply a device for capitalizing early losses, and any loss of use of money during development may be given consideration in arriving at the fair annual rate of return.

Mr. Hamilton estimated going value by "just taken ten per cent of the physical value for this particular case, for that item" and "I have not itemized it in any way." He included "the cost of carrying pipe capacity that is idle a portion of the time until you get up to the load for which it was ultimately or for which it was designed."

The testimony shows that about half of this property has been constructed since January 1, 1927, and that a high rate of return has been earned on all of it, both during construction and on any idle part of it, and the cost of maintaining the idle plant has been included in expenses. Further, idle plant is included in the valuations submitted and a current return and depreciation based on it. It would be a clear duplication to include idle plant in the rate base the same as used plant is included and to allow an additional value for interest and depreciation on idle plant.

Further, the testimony clearly shows that the actual experience of this company has been that the plant has been extended to meet demands and no idle lines have in fact been carried.

Mr. Hamilton's estimate is of value rather than cost. "What I have included is the value of the business attached and operating, and yielding a revenue." In estimating value he considered "partially the cost of attaching business." The customers of this pipe-line system are, with very few exceptions, affiliated companies and there would be no cost of convincing those companies that they should buy gas from this pipe line instead of from a competitor.

He included in his estimate of going value the "time of the engineers and others in negotiating the contracts, but that, for a wholesale situation is a small item." While it is a small item he not only allowed for it in going value, but he also allows for engineering, legal and other expenses separately and in addition to going value.

"The largest cost is the excess capacity that you will have to have for a period of three years, while your distributing companies are getting up to a point where they use the amount of gas that the size of the system is predicated on." This assumption is based on the theory that [fol. 159] the plant is not to be reproduced under existing conditions, but under some other conditions. Mr. Hamilton's hypothesis contemplates the destruction and wiping out of all the distribution systems, the substitution of coal and wood stoves for gas heating and cooking appliances, and then a long campaign running over years of time to induce people to throw away their coal and wood stoves and heaters and reinstall gas appliances.

Mr. Hamilton's concept of going value, which consists largely of interest and depreciation which he referred to as "cost of carrying pipe capacity that is idle," is based on the assumption that the longer a pipe is idle the greater becomes its value. In this case $8,898,532 greater.

Mr. Black considered going value "as being the difference between a plant all ready to operate and not operating, and a plant all ready to operate with customers attached." He estimated going value to include the following items:

Books and records.

Organization of the operating company.

Interest and depreciation on idle plant.

Mr. Black adopted the same theory as Mr. Hamilton in relation to cost of carrying idle plant. The overlapping of estimates is apparent. The estimates both include interest and depreciation on idle plant.

In considering the allowance for going value, we must take into consideration the general nature of the pipe-line company's business as disclosed by the general testimony of the witnesses. For the purpose of arriving at the reasonableness of the rate charged by the pipe-line company we are considering the reproduction of the pipe line and not the distributing plants. The distributing plants were available in most instances before the pipe line was con-

structed, having been placed there for the distribution of local gas and gas from other sources. If the pipe line system were to go out of business and be reproduced, the distributing plants would still be available. The cost of attaching distributing companies to a pipe line does not compare with the cost of acquiring and attaching customers to a distributing system. To a great extent, the burden of acquiring and attaching new customers is placed upon the distributing plants and not upon the pipe line company. From a consideration of all the testimony and the evidence we cannot find any great value to be placed upon going value in a pipe line system situated as the one now under consideration. We find, therefore, that $2,000,000 is an ample allowance for going value based upon the general [fol. 160] testimony of the witnesses, giving consideration to the inclusion by the witnesses of interest and depreciation on idle plant and the very apparent fact that a large number of the elements of going value have been considered and included in other items of value.

The Fair Value of Gas Leases Used and Useful

The company owned as of September 1, 1931, gas leases covering 1,262,361 acres of land situated in Kansas, Oklahoma, Missouri and Texas. (Ex. 40.)

These leases grant to the lessee the right to drill for and take oil and gas, and generally (with some exceptions), run for a period of ten years from date, after which, if oil or gas is not then being produced they expire, otherwise they run so long as oil or gas is produced. The leases in general require the payment of rental until development and require the lessee, after development, to pay to lessors a royalty of one-eighth of the oil and gas. The company owns only the gas rights in these leases, the oil rights being held in most cases by affiliated companies.

These leases have been classified into developed, proven, probable and prospective.

"Developed" leases are those on which gas is actually being produced.

"Proven" are those adjacent to production, which will be drilled and on which it is considered gas will be found.

"Probable" consists of acreage adjacent to proven acreage having favorable geological structure, but which has not been completely tested.

"Prospective" consists of all other acreage. (Davis, Ex. 3, p. 7.)

The acreage owned by the company, and respondents classification of them is as follows (Ex. 40):

	Developed	Proven	Probable	Prospective A	Total
Texas	22,000	72,730	24,647		119,307
Hugoton (Kan. & Okla.)		123,440			123,440
Okla., Kan. & Mo.	20,207		1,000		21,207
Okla., Kan. & Texas				908,287	908,287
	42,207	196,170	25,097	908,287	1,262,361

The same leases (excluding the Kansas, Oklahoma and Missouri, proven and probable) are classified by F. G. Holl, for the Commission, as follows:

Amarillo Field

	Acres	
Proved area:		
Blocked	60,940	
Unblocked	33,767	
Total		94,707

[fol. 161]

Hugoton Field

Proved area:		
Blocked	25,280	
Unblocked	59,087	
Total	85,367	
Probable or semiproved areas	32,008	
Total		116,375

Kansas, Oklahoma, Texas and Missouri

Favorable acreage:		
Kansas	132,202	
Oklahoma	91,317	
Texas	36,326	
Missouri	9,064	
Total		268,909
Prospective acreage:		
Kansas	364,659	
Oklahoma	248,208	
Texas	3,206	
Total		616,073
No value for gas:		
Texas	10,569	
Oklahoma	26,408	
Kansas	80,090	
Total		117,094
Grand Total		1,223,178

NOTE.—Proved and probable leases, Classes 1 and 2, in Kansas, Missouri and Oklahoma are not included in the above, excepting those in the Hugoton field of Kansas and Oklahoma. (Ex. 46.).

The company, ever since its organization, has produced less than half of the gas which it sells. In 1930 it purchased about 54 per cent and produced about 46 per cent.

It owns many gas purchase contracts which entitle it to the gas produced from certain leases in Kansas, Oklahoma, and Missouri, covering 782,421 acres of land and 1,502 wells.

The gas wells situated on the lands covered by these purchase contracts, the gas from which the company is entitled to take by paying the agreed price per M. c. f., have an open flow of gas of 2,138,170 M. c. f. per day (Ex. 3, Tables 16, 17).

The company claims that the fair market value of the gas rights in all of the leases owned by it is $12,914,189, exclusive of the value of the wells and equipment, while the evidence of F. G. Holl, for the Commission, places their fair market value at $4,473,659 (exclusive of the value of the proven and probable Kansas, Oklahoma, and Missouri lease, which the company places at $442,940), so that to obtain a comparable figure, there should be added to Holl's valuation $442,940, making his valuation $4,916,599.

The values of the leases given above do not include the [fol. 162] value of the wells and equipment of wells on developed leases, as claimed by the company at $1,953,149, and as here adopted at $1,811,596.

Of the 1,262,361 acres of leases owned by the company only 42,297 acres have been drilled or developed. The remaining 1,220,064 acres have not been drilled and are undeveloped.

Amarillo Field

(Texas)

The company owns gas leases covering 94,829 acres in what is known as proven sweet gas area in Texas, in the Amarillo field. This proven sweet gas area is a portion of a huge field in the Panhandle, and is approximately 130 miles long and from seven to forty miles wide. It contains approximately 1,001,785 acres.

Of the company's acreage in this field 22,090 acres are developed, having sixty gas wells thereon. The testimony of Ralph E. Davis, the company's witness, a gas engineer and geologist, who made a survey of the company's gas

holdings, is that the recoverable gas (gas reserves) from these leases situated in this proven area, and comprising 94,820 acres, is 15,000,000 cu. ft. per acre.

One of these Texas leases is the Burnett lease (Ex. 48). It covers 63,880 acres, and requires a minimum payment of $50,000 per year, in advance, for ten years whether or not gas is taken from the lease. For the first two years, the royalty is one-eighth of 3 cents per M for all gas taken; for the next three years, one-eighth of 3½ cents per M; for the next five years, one-eighth of 4 cents per M; thereafter one-eighth of 4 cents unless the price of gas at the well is increased, in which event the royalty is to be one-eighth of the weighted average price. The Burnett lease is not a solid block, there being within said lease other leases owned by others than the company, on which there are producing wells. Up to the present time the $50,000 annual payments required on this lease have exceeded the royalty earned on the gas taken.

The witnesses for the company placed the market value of these leases at from $45 to $125 per acre, the higher values being placed on the Burnett ranch and blocked acreage. Eight witnesses testified for the respondents, two of them were employees, and all of the remaining, save one, were connected with companies whose interest it is to place a high value on leases for rate-making purposes.

F. G. Holl, for the Commission, testified that the value of the blocked acreage, consisting of 60,940 acres, was $45 per acre, and that the value of the remainder of the proven [fol. 163] leases 33,767 acres, was $25 per acre. Holl testified that scattered leases in this field in Wheeler county in the vicinity where the largest wells in the entire field have been found could be purchased at $5 per acre, net to the purchaser, such leases covering both the oil and gas. That in Potter county, near where the largest wells have been found, on September 14, 1931, a lease which was about to expire was renewed at $8 per acre for 5,000 acres.

The evidence of respondents shows that in 1931 the company conveyed to the Texoma Natural Gas Company (an affiliated company) 59,788 acres of leases, including the Coon ranch of approximately 25,000 acres, which was blocked, at the price of $45 per acre. This acreage was all in the proven sweet gas area in the Amarillo field, and is comparable with the proven and developed leases retained

and now owned by the company. The evidence also shows that these leases so sold to the Texoma cost the company somewhat less than $15 per acre on the average. (Ex. 34, Tr. 454, 455.)

The books of the company also show that from January 1, 1930, to June 30, 1931, it purchased 21,158 acres of its leases in the Amarillo field in the sweet proven gas area, now valued by respondents at approximately $93 per acre, at an average cost of but $12.78 per acre. (Ex. 90.)

The evidence shows that there is a large oversupply of gas developed by gas companies and independent producers in the Amarillo field, which on account of the lack of market, cannot be sold, and that gas is being sold in this field at 2 cents per M. c. f. at the well. That in the Amarillo proven sweet gas area there are approximately 125 "shut-in" wells drilled and capable of producing gas which cannot be sold for want of a market, and that these "shut-in" wells have an open flow of 2,260,000,000 cu. ft. per day.

That the owners of wells are able to sell only a small per cent of their gas; that the Lone Star Gas Company has a pipe line into this field connected to 65 wells, from which the runs averaged during the first six months of 1931, a little over 100 M per day, for which the company paid 2 cents per M, or a royalty of $2 per day (less than interest on the cost of completing a well), and for that reason operators are not drilling any more wells or acquiring any more acreage. (Tr. 1920, 1921.)

From all of which we conclude and find that the fair market value of the developed and proven gas leases in the Amarillo field, owned by the company, as of September 1, 1931, does not exceed the following:

[fol. 164] Fair Market Value Leases—Amarillo Field

[fol. 164] Developed and proven:	Acreage	Value per acre	Fair market value
Blocked acreage	60,940	@$50	$3,047,000
Not blocked	33,880	@ 35	1,185,800
Totals	94,820		$4,232,800

Probable Acreage

The company owns 24,547 acres of gas leases in Texas situated outside of the proven sweet gas area, some of which are in the sour gas area.

The testimony of the witnesses for respondents as to the value of this acreage varied. Some stated that part of these are worthless (Freeman p. 593); others at from $5 to $25 per acre.

F. G. Holl, for the Commission, placed the fair market value of the gas rights in that part of this acreage which he classed as "favorable" at $1 per acre and 50 cents per acre for that part which he classes as "prospective," and nothing for the remainder of the Texas acreage. (Ex. 46.).

We find from the evidence that the average fair market value of the gas rights for this 24,547 acres classed by respondents as "probable" does not exceed $2 per acre, and that the fair market value of such acreage does not exceed $49,094.

Hugoton Field

(Kansas and Oklahoma)

The company owns 123,440 acres of gas leases in the Hugoton field situated in northwestern Oklahoma and southwestern Kansas, all of which it contends are "proven." (Ex. 40.)

This is another enormous gas field estimated to comprise 4,000,000 acres of gas-productive lands. Its limits are not yet defined. They can be determined only by additional drilling. Dr. Raymond C. Moore, state geologist, estimates the gas reserves in this field as sufficient to supply all of the state of Kansas, on the basis of that now used in Kansas, for a period of over 100 years. (Tr. 1964, Ex. 47.) There is a market for but a small portion of the developed gas in this field. Little drilling has been done, but there is sufficient drilling to demonstrate that this is a rich field of gigantic proportions.

Of the company's acreage, F. G. Holl, for the Commission, classified 84,367 acres as "proven," 32,008 acres as "probable" and the remainder as "prospective."

[fol. 165] Ralph E. Davis, for respondents, gave it as his opinion, as a result of his geological survey made for respondents, that the recoverable gas from the "proven" area of this field is 10,000,000 cu. ft. per acre, and from the "probable" at 7,000,000 cu. ft. per acre. (Table 1, Ex. 3.)

There is no development and no wells on any of the company's acreage in the Hugoton field. The company's leases

consist of one large lease, the Stonebreaker lease, covering 25,280 acres, and over 500 smaller leases. The terms of each of these 500 leases require the drilling of a well within ten years from its date; otherwise, the lease expires at the end of ten years. The cost of a well in this field is over $25,000, and if the company is to hold these leases it will have to drill at least 500 wells within eight years from this date, that is, before 1940, at a cost of $12,500,000, or said leases undrilled will expire. The company has no pipe line within ninety miles of these leases. (Tr. 1019.)

Witnesses for respondents, four in number, testified that the fair market value of the gas rights in these leases, which are in the proven area, is from $3 to $10 per acre, and the respondents claim that the fair market value of their 123,440 acres of leases is $1,172,680.

Against this is the testimony of F. G. Holl that leases for oil and gas could be purchased in the proven area of this field at the time of the hearing at $1 to $2 per acre; that the Derby Oil Company had within sixty to seventy days prior to his testimony, purchased 5,947 acres of leases in this proven area at $1 per acre (Tr. 1958) and that the fair market value of these leases is:

Hugoton Field

Proved area:	Acres	Per acre	Fair market value
Blocked	25,280	@$7 50	$189,600 00
Unblocked	59,087	@ 1 50	88,630 50
Probable area	32,008	@ 1 00	32,008 00
Prospective area	7,065	@ 50	3,532 50
Totals	123,440		$313,771 00

We find that the fair and reasonable value of this 123,440 acres is not in excess of the following:

Fair Market Value Leases—Hugoton

	Acres	Per acre	Fair market value
Proven (blocked)	25,280	@$7 50	$189,600 00
Proven (not blocked)	59,087	@ 5 00	295,435 00
Probable	32,008	@ 2 00	64,061 00
Prospective	7,065	@ 1 00	7,065 00
Totals	123,440		$556,116 00

[fol. 166] Kansas, Oklahoma and Missouri

(Exclusive of Hugoton Field)

Proven and Probable

Ross Stuntz, superintendent for the company, testified that the company owned, in Kansas and Oklahoma, proven and developed and probable acreage, of the fair market value as follows (Tr. 717-719):

Proven and developed:	Acres		Fair market value	
Kansas	16,125		$138,240	
Oklahoma	4,082		239,700	
Totals		20,207		$377,940
Probable acreage:				
Kansas	80		$8,000	
Oklahoma	980		57,000	
		1,000		65,000
Totals		21,207		$442,940

(Tr. 935)

There was no other evidence as to the value of this acreage, and it is accepted as correct.

Prospective Acreage

This acreage is scattered throughout Texas, Oklahoma, Kansas and Missouri. Very little of it is within the reach of the company's pipe lines. From its location it is probable that its value, if any, is for oil and not gas.

From July 1, 1931, to October 1, 1931, the company surrendered 61,471 acres of prospective acreage, as not of sufficient value to warrant payment of rentals. (Ex. 43.)

The acreage of the company's prospective leases, as classified by Mr. Nesbit, chief geologist for respondents, is 998,287 acres, which he values at $2 per acre. (Ex. 30.)

Ralph E. Davis, for respondents, classifies 1,031,127 acres of the company's leases as "prospective" and values them at $1 per acre.

F. G. Holl, for the Commission, classifies 268,909 acres as "favorable" and values them at $1 per acre, 616,073 acres as "prospective" at 50 cents per acre, and the remainder at no value.

The foregoing being for the gas rights only.

It is our conclusion that the value of the gas rights in these prospective leases is not in excess of $998,287.

The following is a summary of what we believe the fair weight the evidence shows is the classification of all of the gas acreage of the company. We also find that the fair [fol. 167] value of all the acreage of the company, exclusive of the value of the wells and well equipment, is not in excess of the amounts set forth below.

Summary

Fair Market Value of Gas Leases

	Acres	Value per acre	Fair market value
Amarillo Field (Texas):			
Developed and proven:			
Blocked	60,940	@$50.00	$3,047,000
Not blocked	33,880	@ 35.00	1,185,800
Total	94,820*	.....	$4,232,800
Probable acreage	24,547	@ 2.00	49,094
Total	119,367	.....	$4,281,894
Hugoton Field (Kansas and Oklahoma):			
Proven blocked	25,280	@ $7.50	$189,600
Not blocked	59,087	@ 5.00	295,435
Probable	32,008	@ 2.00	64,016
Total	116,375		
Prospective	7,065	@ 1.00	7,065
Total	123,440	.....	$556,116

* Of the above, 22,090 acres are developed with sixty producing wells.

	Acres	
Kansas, Oklahoma and Missouri (exclusive of Hugoton):		
Proven:		
Kansas, Oklahoma and Missouri	20,207	$377,940
Probable:		
Kansas, Oklahoma and Missouri	1,060	65,000
Total	21,267	$442,940
Prospective:		
All other except Hugoton	998,287	998,287
Total	1,262,361	$6,279,237

The value of all leases of the company, after deducting the value of leases canceled and surrendered, as shown by the books of the company, is (book value) $6,573,489.70. (Tr. C. H. Montgomery, Ex. 49.) Add value of wells and

well equipment, $1,811,596; total value of all leases and wells, $8,090,833.

Gas Leases—Used and Useful

The amount of gas produced and purchased by the company for the year ending December 31, 1930, is as follows (Ex. 3, Table 10, p. 65):

Gas purchased and produced:	M. c. f.
Gas produced	34,401,978
Gas purchased	31,123,002
Residue gas purchased	8,638,965
Total	74,163,945
Or on an average per day of (74,163,945 ÷ 365)	203,189

[fol. 168] This is on an 8-oz. base, to reduce to a 2-lb. base, on which the measurement of the gas produced is based, this amount should be reduced by 9.2 per cent.

The peak load of the company's gas system was on January 16, 1930. On that day the companies used 330,000 M. c. f. of gas. (Tr. 905.)

The pipe lines of the company have no greater capacity than for this peak load (Tr. 244, 252) and there is little probability of any greater demand for gas than that produced and purchased by the company in 1930, for the reason that because of local gas, and the proximity of other pipe-line companies, the company's opportunity to extend its territory is limited.

The evidence shows that the company in the past and at the present time buys more gas than it takes from its own leases. In 1930 the company purchased about 54 per cent and produced about 46 per cent of the gas sold.

Gas Reserves

The company owns purchase contracts for gas on leases in the Kansas and Oklahoma fields adjacent to its pipe lines which have wells, the open flow production of which is 2,138,170 M. c. f. per day. (Ex. 3, Tables 16 and 17.)

These purchase contracts cover 782,421 acres of leases and 1,502 gas wells. The total open-flow capacity per day

of the gas wells owned by the company, plus the gas to which it is entitled under its purchase contracts, is:

Open flow per day:	M. c. f.
Amarillo, 60 wells, 22,090 acres (Tr. 449)	1,532,625
Kansas, Oklahoma and Missouri, 20,207 acres (Ex. 3, Table 3)	258,837
Add purchase contracts (Ex. 3, 82-96, Tables 16, 17)	2,138,170
Total open flow (available to company)	3,929,632

The foregoing, 3,929,632 M. c. f., is the open-flow capacity per day of the wells owned by the company from 42,297 acres, all of its developed leases, plus the daily open-flow capacity of the wells situated on the leases covered by its purchase contracts.

The amount of gas which it is customary to take and which can be safely taken from a well is 20 per cent of its open-flow capacity, so that the amount of gas which is daily available from the company's purchase contracts and producing wells is 20 per cent of the daily open-flow capacity, or 785,926 M. c. f., which is more than 3½ times the average daily consumption of gas produced and pur- [fol. 169] chased and more than 2½ times the highest peak load and capacity of the company's pipe-line system.

From the foregoing it will be seen that the company now has available from its purchase contracts and from its developed leases in Kansas, Oklahoma, Missouri and Texas (42,297 acres of leases) 786,309 M. c. f. of gas per day, over 3½ times its average daily requirements, and 2¼ times its maximum requirements on the day of its peak load.

This leaves the company a reserve of 1,220,064 acres of leases which are undrilled, unused, and are not called upon to meet the company's requirements, as follows:

Undeveloped leases:	Proven	Probable	Prospective	Total
Texas	72,730	24,547	.....	97,277
Hugoton	123,440	.....	.....	123,440
Oklahoma	.....	980	.....	980
Kansas	.....	80	.....	80
All other	.....	.....	998,287	998,287
Total reserve acreage not developed or used				1,220,064

None of these 1,220,064 acres is drilled or producing. The Hugoton field, where the company owns 123,440 acres of undrilled proven leases (its classification) is approximately ninety miles from the company's pipe line. The number of separate leases in this field is over 500, all of which will expire in eight years unless drilled. This means that to hold these leases the company will have to drill over 500 wells at an expense of over $25,000 per well, or over $12,500,000, within the next eight years, and in addition pay a yearly rental in a substantial amount.

Prospective Leases

The leases of the company classified by it as "prospective," consisting of 998,287 acres, are scattered. Very few are available to the company's pipe line.

Ralph E. Davis, geologist and gas engineer, witness for the company, who made an exhaustive study of the company's holdings, testified that the recoverable gas reserves in the company's leases in the Amarillo field is 15,000,000 cu. ft. per acre for the probable. In the Hugoton field, 10,000,000 cu. ft. per acre for the proven and 7,000,000 cu. ft. per acre for the probable, and stated that these figures are conservative. (Ex. 3, pp. 25, 27.)

On this basis, if the classification of Mr. Davis of the acreage is accepted, the gas reserves of the company in the acreage covered by the company's gas leases classified by [fol. 170] Mr. Davis as proven and probable, amounts to 2,448,664,000 M. c. f. (Ex. P. 34, Table 1, p. 36), exclusive of the 998,287 acres of leases classified by the company as "prospective."

If it be assumed that the company will annually require in the future as much gas in addition to that purchased as it required in the year 1930, its annual requirements from its gas leases would be 34,401,978 M. c. f. (Ex. 3, p. 65, Table 10), and its recoverable gas reserve represented by its leases, proved and probable, excluding all the prospective, would last for seventy-one years, plus.

On the same basis, the company's holdings in the Amarillo field alone would supply all of its requirements for fifty years, plus.

Or, if the company should disregard its purchase contracts and purchase no gas and take all of its requirements,

which for 1930 amounted to 74,000,000 M. c. f. (Ex. 3, p. 65, Table 10), from its proven and probable leases, its recoverable gas reserve, excluding its prospective leases, would last for thirty-three years, plus.

Or, if the company would surrender all of its leases except only the proven and probable, in the Amarillo field, and would cancel all of its purchase contracts, its Amarillo leases alone would supply all its requirements, 74,000,000 M. c. f. per year for twenty-three years, plus.

$$\frac{\text{Total gas reserve (excluding gas purchased)} \quad 2{,}448{,}664{,}000 \text{ M. c. f.}}{\text{Total gas produced, 1930} \quad 34{,}401{,}978 \text{ M. c. f.}} = 71 + \text{years}$$

$$\frac{\text{Total Amarillo reserve (excluding gas purchased)} \quad 1{,}726{,}650{,}000 \text{ M. c. f.}}{\text{Total gas produced, 1930} \quad 34{,}401{,}978 \text{ M. c. f.}} = 50 + \text{years}$$

$$\frac{\text{Total gas reserve (excluding gas purchased)} \quad 2{,}448{,}664{,}000 \text{ M. c. f.}}{\text{Total gas sold 1930 (Including gas purchased.)} \quad 74{,}000{,}000 \text{ M. c. f.}} = 33 + \text{years}$$

$$\frac{\text{Total Amarillo reserve (excluding gas purchased)} \quad 1{,}726{,}650{,}000 \text{ M. c. f.}}{\text{Total gas sold 1930 (Including gas purchased.)} \quad 74{,}000{,}000 \text{ M. c. f.}} = 23 + \text{years}$$

If the opinion of Mr. Nisbit, respondents' geologist, as to the classification of the acreage of the Hugoton field as to proven and probable, is accepted the amount of the company's gas reserve will be greatly increased as he classifies 123,440 acres in the Hugoton field as "proven," while Mr. Davis classified the company's holdings in the Hugoton field as 49,210 proven, and 28,070 as probable.

From the foregoing it will be seen that the company owns many more gas leases than are "used and useful" in the business of supplying gas to its consumers. It is a fair inference from the facts in evidence that the company acquired these excess leases expecting to sell them at an enhanced price. The evidence shows it did this in the sale [fol. 171] of 59,788 acres of leases to the Texoma in 1931, at a profit of over $1,000,000.

Of the leases owned by the company, 123,440 acres valued by respondents at $1,172,680 are in the Hugoton field. None of them is producing, none have been drilled. They are all approximately ninety miles from any pipe line owned by the company. The terms of the leases require the expenditure of over $12,500,000 within eight years for drilling to prevent their expiration, and also require the pay-

ment of a substantial amount yearly in rentals. The acquisition of these leases at the price the company paid for them was no doubt a wise business venture on which, when these leases are sold, a substantial profit should be realized, but they are not used or useful to the company in supplying the needs of its customers, nor can it be seen that they will be in the near future.

The same can be said of the 998,287 acres of nonproducing leases designated as "prospective." They are scattered, their value is speculative, very few are available to any pipe line owned by the company, and they are a source of expense in annual rentals.

In fact the company recognizes this fact as the evidence shows that it released and surrendered 61,471 acres of these leases between July 1, and October 1, 1931, as not worth the stipulated rentals.

The following gas acreage, consisting of 50,000 acres in the proven sweet gas area in the Amarillo field, 22,090 acres of which are developed, and all of the proven, developed and probable acreage situated in Kansas, Oklahoma and Missouri, 21,267 acres are, in our opinion, the only leases of the company which are used and useful and are sufficient for all the company's present requirements and for a sufficient reserve.

Used and Useful Leases

	Acres		Fair market value	Gas reserve M. c. f.
Kansas, Oklahoma and Missouri:				
All developed, proven and probable leases in Kansas, Oklahoma and Missouri	21,267		$442,940	35,424,000
Texas-Amarillo Field:				
Blocked	45,830	@$50	2,291,500	.....
Not blocked	4,170	@ 35	145,950	750,000,000
Total	71,267		$2,889,390	783,424,000

Of these 71,267 acres, 42,297 are producing and 28,970 acres are not developed, as follows:

Proven Leases:	Acres	
Developed:		
Texas	22,090	
Kansas, Oklahoma and Missouri	20,207	
Total		42,297

[fol. 172]

Undeveloped:		
Texas—proven	27,910	
Oklahoma—probable	980	
Kansas—probable	80	
Total		28,970
Total		71,267
Total fair value of all leases (71,267 acres used and useful)		$2,880,390
Add value of all wells and well equipment		1,451,626
Total value of leases, used and useful, including wells and well equipment		$4,332,016

The gas reserve in these 71,267 acres according to respondents' testimony is 783,424,000 M. c. f. This is sufficient to furnish all of the company's requirements in addition to the gas purchased under its purchase contracts, on the basis of its requirements for the year 1930, for a period of 22 years, plus, as follows:

Gas Reserves in 71,267 Acres Allotted to the Company as Used and Useful

	Acres	Gas reserve per acre	Amount of gas reserve M. c. f.
Amarillo proven	50,000	15,000 M	750,000,000
Kansas, Missouri and Oklahoma, proven and probable	21,267	.....	33,424,000
Total gas reserve	71,267	.....	783,424,000

(Ex. 3, pp. 25, 26, 27, 35.)

$$\text{Gas reserve 71,267 acres: } 783{,}424{,}000 \text{ M. c. f.} \div \text{Yearly requirement: } 34{,}401{,}978 \text{ M. c. f.} = 22 \text{ years, plus}$$

The sixty wells on the 22,090 acres in the proven sweet gas area in the Amarillo field included in the acreage allotted to the company as above, are capable of supplying 306,525 M. c. f. per day (20 per cent of open flow—1,532,625 M. c. f. ÷ 5 = 306,525 M. c. f.)

The maximum capacity of the company's pipe line from the Amarillo field, a 20-inch line, is but 125,000 M. c. f. per day. In other words, the sixty wells on the 22,090 de-

veloped acres in Amarillo field are capable of supplying over twice as much gas as the company has pipe-line capacity to take from the Amarillo field.

In arriving at the value of these 71,267 acres of leases allotted to the company as "used and useful" the fair market value of the Kansas, Oklahoma and Missouri acreage, as claimed by respondents in exhibit 40, is adopted.

These 71,267 acres here allotted to the company as used and useful include all of the company's developed leases, [fol. 173] wherever situated; also all of its proved and probable leases in Kansas, Oklahoma and Missouri (except the Hugoton field).

We find that all other leases owned by the company (1,220,064 acres) are not used and useful to the company in supplying gas to its customers. It would be inequitable to include the value of leases other than the 71,267 acres specified above, owned by the company in the rate base, or to charge, as costs of operation, the expense of carrying such excess leases.

The amount of gas reserve which a company should be allowed to carry for valuation purposes is best determined by its requirements. The records in this case are quite complete as to the requirements of the company. A gas company should not be allowed to speculate in gas leases and have its speculation financed by charges to its consumers. Neither should it be allowed to place in its valuation for the purpose of increasing its return, gas reserves over and above those necessary to serve properly its consumers. The gas company at a small cost has acquired gas rights which it now claims have a value of millions of dollars. We are interested only in those which are used and useful in the public service. We cannot see how any leases other than the 71,267 acres of leases designated above can be held to be used or devoted to the public service.

In the United Fuel Gas Company case the company asked that the value of its gas rights and leaseholds be fixed at $30,000,000. It was given a value of approximately one-fifth of that amount, based on the book value in the absence of any better evidence in the record.

In speaking of the value of the gas leases the court in the United Fuel Gas Co. v. Public Serv. Com., 14 F. 2d 209, said:

"The plaintiff, at a net cost of a few millions acquired rights which it claims have now a value of upwards of thirty, and which it might be difficult to deny were worth two-thirds of that sum. What proportion of this is presently used and useful in the public service? Roughly, four-fifths of the valuation it puts upon them is represented by gas which upon reasonable grounds it believes to be under land in which it has not yet operated and nearly two-thirds under acreage underneath which it has not yet been demonstrated that there is any gas, although its presence there is probable. Plaintiff is not to be criticized for acquiring these rights widely extended and largely untested as they are. In securing them it doubtless acted wisely, both from its own standpoint and from that of those who depend upon it for their supplies of gas. But is that of any present importance?

"It will be noted that the total of the gas underlying the proven acreage was 249,100,000 M. c. f. As the plaintiff [fol. 174] sells annually about 47,000,000 M. c. f., of which 10,500,000 goes to the West Virginia retail purchasers, it has under its proven territory gas enough for everybody for more than *five years*, and an amount sufficient to meet the needs of its public-service patrons alone for almost a quarter of a century.

"For the reason already stated, we cannot see how any other portion of its gas can be held to be used in the public service, no matter how elastic a definition be given to the word 'used.' At the risk of tiresome repetition, we can say that we do not criticize plaintiff for acquiring any or all of its gas rights. It was doubtless wise to get them. All that we decide is that, in arriving at the rate base upon which plaintiff is entitled to a fair return, we may not combine two opposing theories." (Italics ours.)

Neither do we criticize the pipe-line company for acquiring these gas leases. Their purchase was no doubt a wise speculation and the sales to the Texoma Natural Gas Company prove them to have been profitable, but property acquired for speculative purpose should not enter into the rate base. We find the fair market value of the gas leases (exclusive of wells and well equipment) used and useful in the system to be $2,880,390.

Valuation Summary

The following is a summary of all the accounts entering the rate base:

Acct. No.	Title	Cost of reproduction	Reproduction cost less depreciation
1307	Production rights of way	$55,982	$55,982
1310	Production field measuring station structures	40,517	35,909
1311	Production other structures	59,087	47,876
1312	Production gas well construction	1,588,450	1,153,157
1313	Production gas well equipment	894,618	658,439
1314	Production field line equipment	3,548,102	3,126,159
1315	Production field measuring station equipment	302,611	205,746
1316	Production drilling and cleaning equipment	32,833	27,908
1317	Production other equipment	1,637	1,333
1325	Transmission land	145,202	145,202
1327	Transmission rights of way	1,057,530	1,057,530
1328	Transmission compressing station structures	1,608,151	1,406,102
1329	Transmission measuring station structures	147,337	133,310
1330	Transmission other structures	128,704	113,341
1331	Transmission compressing station equipment	8,954,220	8,048,910
1332	Transmission measuring station equipment	820,281	759,025
1333	Transmission line equipment	43,740,208	39,432,331
1334	Transmission other equipment	6,938	5,633
1376	General other land	3,055	3,055
1379	General other structures	117,306	94,687
1380	General office equipment	117,817	106,035
1381	General store equipment	2,123	1,805
1382	General shop equipment	26,991	23,084
1383	General stable equipment	640	568
1384	General garage equipment	104,391	81,448
1385	General laboratory equipment	8,369	8,202
1386	General telephone and telegraph system	484,926	415,070
1387	General tools and implements	51,358	44,979
1388	General other equipment	23,877	21,832
	Subtotals	$64,809,107	$57,935,858
	Preliminary and organization expense	480,008	480,008
	Engineering and superintendence during construction	3,218,585	2,881,000
	Administration and legal expense during construction	340,094	304,084
	[fol. 175]		
	Taxes during construction	875,171	778,044
	Interest during construction	4,351,934	3,883,282
	Miscellaneous construction expenditures	680,187	608,169
	Cost of financing		
	Working capital	775,000	775,000
	Materials and supplies	509,400	509,400
	Going-concern value	2,000,000	2,000,000
	Totals	$78,052,486	$70,176,845
	Gas leases	2,874,390	2,874,390
	Grand totals	$80,926,876	$73,051,235

Annual Depreciation and Depletion Requirements

The respondents claim a total of $3,276,325.07 as an allowance for annual depreciation and depletion requirements. Of this amount $2,183,555 was claimed as the necessary allowance for physical equipment other than gas leases. An amount of $1,092,770.07 was claimed as a necessary allowance for annual reserve requirements pertaining to gas leases.

Requirements for Physical Equipment Other Than Gas Leases

Exhibit 27 sets forth the amounts claimed for annual depreciation covering each classification of physical property. By comparing these amounts with the cost to reproduce new the physical property as set forth in Mr. Hamilton's exhibit, we have found the annual percentages as applies to each classification of property as claimed by the company are as follows:

		Per cent
Production	field measuring stations	9.36
Production	other structures and equipment	5.43
Production	gas well construction and equipment	6.25
Production	field line equipment	7.25
Production	drilling and cleaning equipment	10.00
Transmission	rights of way	2.47
Transmission	other structures	3.71
Transmission	measuring stations	3.39
Transmission	compressing station structures	3.09
Transmission	compressing station equipment	2.90
Transmission	line equipment	2.35
Transmission	other equipment	5.00
General	other structures	6.71
General	office equipment	
General	store equipment	
General	shop equipment	
General	stable equipment	
General	laboratory equipment	
General	tools and implements	
General	other equipment	
Average, per cent		3.01

It will be noted that these percentage allowances range from 2.35 per cent to 10 per cent. 2.35 per cent is the allow- [fol. 176] ance claimed for the pipe line and this figure is supported by the testimony that some of the main pipe lines have a life of over fifty years and are extended into the Amarillo field, which has a sufficient reserve to supply the lines for a period equal to their lives.

The percentage allowances as claimed by the respondents are not disputed by the evidence. We have accepted such percentages and applied them to the present cost of reproduction as found by us. By applying these percentages to the values which we find, we have calculated that the annual allowance for depreciation of physical property would be $1,894,022, based on physical property values at September 1, 1931.

However, the value of the physical property at September 1, 1931, is not a basis for the measure of depreciation during the years ended December 31, 1930, and June 30, 1931. As is pointed out in the discussion herein relating to the rate base and the average values which should be included in the rate base for comparison with the return earned during a stated period, the annual allowance for depreciation should be based upon the average value of the physical properties during the earning periods under consideration.

In this instance the annual allowance for depreciation should be based on the average value during the year ended December 31, 1930, and the average value during the year ended June 30, 1931, calculation of which is hereinafter set out.

We have applied the annual rates for depreciation, set forth above, to the physical property values which we have adopted herein as at September 1, 1931, and have found the weighted average rate of 2.96 per cent. Applying this percentage to the average value of physical properties for the year ended December 31, 1930, we find the depreciation allowance for that year should be $1,693,312, and in like manner have found the depreciation allowance for the year ended June 30, 1931, to be $1,712,216, which gives us an average depreciation allowance for the two-year period covered by the investigation of $1,702,764.

Requirements Pertaining to Gas Leases

The respondents claim an allowance for annual reserve requirements pertaining to gas leases as follows:

General development expenses capitalized	$532,530.77
Amortization of nonproducing leases	314,981.68
Dry-hole expense	174,747.74
Depletion of producing leases	70,509.88
Total	$1,092,770.07

These will be discussed in their order.

[fol. 177] General Development Expense—Capitalized

The company asks for a reserve allowance of $532,530 for general development expense capitalized.

Mr. Eastman testified that this item includes the following character of expenditures:

Cost of acquiring leases.
Geological expense.
Lease rentals.

The cost of acquiring leases was made up of salaries and expense of men engaged in acquiring leases and scouting expenses.

The item of $532,530 represents the expenditures for leasehold development charged to capital investment during 1930. These general development expenses are capitalized and also charged off through the reserve during the same year. The result would be the same if these expenditures were charged directly to an expense account. The general development expenses are not charged off each year on the books. Some rentals paid on leases sold to the Texoma Company are included in this amount.

The practice of the company is to charge expenditures for general development to fixed capital currently as such expenditures are made. Then, annually, the aggregate of such expenditures during the year are charged to expenses and included in expenses for that year, and the same amount credited or added to the reserve for depreciation and depletion. Under this practice the general development expenses are not charged off on the books each year,

but are accumulated from year to year in fixed capital account and if the company followed this practice consistently, a like accumulation would be made in the depreciation and depletion reserve.

The effect of this practice is to include in expense each year the total development expenses and also to include them in fixed capital accounts, the latter being offset by the reserve for depreciation and depletion.

The cost of acquiring leases, including geological and scouting expenses, are capital expenditures. They go to make up the present value of the leases upon which a return is allowed. When a field starts producing, the items mentioned above are part of the value of the lease which is charged off during its producing life and return of capital is provided for under the allowance for "depletion of producing leases." If the cost of acquisition and other expenses enumerated above are included in the annual allowance for depletion, and if in addition a return is allowed on the value of the leases, which includes these expendi- [fol. 178] tures, there would then be a duplication of charges. That is, the expenditures would be included in expenses in the first instance and included in the rate base for a return in the latter.

The value of the leases as found by the Commission is the present fair value which includes among other elements, the cost of acquisition, scouting, and geological expense, and to include such expenditures in an allowance for annual depletion would result in returning the company its investment the same year the expenditure was made while including it in the rate base for the purpose of a return.

We conclude, therefore, that all the items which make up the $532,530, with the exception of annual lease rentals, are a duplication and should be excluded from the annual allowance for depletion as it is covered by the present value of the leases and so included in the rate base. All of this item, with the exception of annual lease rentals, should also be excluded for the reason that the evidence shows that the undeveloped gas reserves assigned to the company consists of 28,970 acres of leases, all of which except 1,060 probable are proven and which, therefore, will not require any development such as scouting, geological investigation and the other expenses going to make up this item.

An allowance for annual lease rentals presents a much more difficult question. It is doubtful whether or not any such allowance should be made. The matter was covered in Re United Fuel Gas Company, P. U. R. 1924A, 357, 366, where it was said:

"There never was and there is not now any good reason why the consumer should pay the royalties and delay rentals. The royalties and delay rentals are for the purpose of carrying the investment of the company in its gas. The gas belongs to the company and it should take care of the royalties and delay rentals in the same manner as it would take care of the interest on its bonded indebtedness. The delay rentals are for the purpose, as stated above, of extending the life of the undeveloped leases. The company may take such leases and surrender them at will and the consumer has no remedy against such conduct on the part of the company. If the consumers have no rights in the premises, they should not be compelled to furnish a fund with which the company may gamble at will. The question of taking, carrying and surrendering gas leases is one that appeals direct to the sound discretion of the managing officials of a gas company and their responsibility should be impressed upon them by compelling the company, and not the consumers, to pay these delay rentals."

Because we have included 1,060 acres of gas reserves in Kansas and Oklahoma, as used and useful, due to their ad-
[fol. 479] vantageous location, we are inclined to make an allowance sufficient to cover lease rentals on such acreage.

We have found 71,276 acres of leases of which 28,970 acres are now developed or producing to be used and useful. No rentals are paid on producing leases. 27,910 acres of the undeveloped leases are located in the Amarillo proven sweet gas field and the remainder, amounting to 1,060 acres, are situated in Kansas and Oklahoma. The undeveloped leases which are assigned to the company and which are situated in the Amarillo field, and which are undeveloped, are in a block acreage, and are in what is known as the Burnett lease on which an annual guaranteed royalty of $50,000 a year is required to be paid, in lieu of annual rental, which annual guaranteed royalty is charged by the company as an expense of operation. For this reason, no additional

allowance should be made to the company for rental on these leases. This leaves 1,060 acres in Kansas and Oklahoma which are undeveloped and on which a rental will be required to be paid. There is no evidence in the record showing exactly the amount of rental which must be paid to hold these undeveloped leases in Kansas and Oklahoma, but as in general the leases which have been introduced in evidence show that the rental which is required to be paid until development is made is, in no case, more than $1 per acre per year, we assume that the rental on these leases is that amount and we, therefore, allow for annual rental on these leases the sum of $1,060. This $1,060 we find is the only amount which should be allowed for this account.

Amortization of Nonproducing Leases

The company seeks to include in its annual reserve allowance an amount of $314,981.68 for the amortization of nonproducing leases.

Mr. Eastman testified that the amount claimed for amortization of nonproducing leases is to provide a reserve to amortize the cost of leases which are nonproducing:

The amount amortized is the purchase price or bonus paid for leases.

For example, in the case of ten-year leases, one-tenth of the purchase price is to be charged to expense each year until the expiration of the lease or until a well is drilled, to amortize its cost over the period of the term of the lease, or over the period of ten years.

The figure of $314,981.68 is taken from the books and covers the year 1930.

The company thus seeks to have included in expenses as [fol. 180] an annual reserve allowance, the cost of leases through the amortization charge, and also asks to have the present fair value of the leases included in the rate base on which to earn a return.

The present fair value of these leases is included in the valuation of the company's property and in the rate base on which these leases will be allowed a return. This value covers not only all the actual costs, including the bonus paid for the leases, but also the additional enhancement in value caused by their appreciation in value as of September 1, 1931. This, in most instances, is many times the actual cost of the lease.

There is, in fact, no depreciation or depletion of an undeveloped lease until it has been drilled and commences to produce gas. As soon as a lease becomes productive annual expense for depletion is allowed and provided under amortization of producing leases. In the meantime the company is allowed a return on not only the cost, but on the full, fair value of the lease, and it is seen, therefore, by this contention the company is asking to have returned both the cost of the leases through an annual reserve charge and also return on the fair market value of the leases, and when the leases become productive to have the full value of the developed leases returned through amortization of producing leases.

If a return is allowed on the fair market value of these undeveloped leases, which includes the bonus paid, we believe that no reserve allowance should be made so long as they are nonproductive.

If the company were allowed one-tenth of the value of these leases annually for ten years it would thus have returned to it in that time the fair value of these leases, amounting to $1,169,500, irrespective of whether the leases were producing, and thus the present consumers would be required to pay for the amortization of these leases although they would have received no gas and no benefit from them. We believe that if the consumers are required to pay a rate for gas based on a return upon the fair value of its properties, including the fair value of these leases, they should not be required also to pay for the amortization of nonproductive leases which are not, in fact, being depleted.

If and when the nonproducing leases expire or are surrendered because they have been found to be nonproductive, then and not until then, is the time when their cost or value should be charged as an expense, and if the lease through development becomes productive, annual depletion is then allowed in the item of depletion of producing leases.

[fol. 181] Even if the contention of the company that it should be allowed an annual expense for amortization of nonproducing leases were conceded to be sound, amortization of such leases based upon the experience of the company for the year 1930 is not a fair measurement of annual

requirement for amortization in future years, commencing with September 1, 1931. This is for the reason that on the findings herein made the company will have as used and useful leases, as of September 1, 1931, only 28,980 of undeveloped leases, valued at $1,460,500, while the company's estimate of $314,981.68 claimed for annual depreciation is based on holdings of approximately 1,220,064 acres of undeveloped leases held by it in 1930, valued by it at over $10,000,000.

In the allowance to the company for nondeveloped leases which are used and useful, as herein found, there are 27,910 acres which are conceded to be proven and only 1,060 acres are classified as probable, and it is improbable that any of these leases will be surrendered or permitted to expire.

We find that there should be no allowance for this account.

Dry-hole Expense

The respondents ask for an annual allowance or reserve in the amount of $174,747.74 for dry-hole expense. This figure is based upon the experience of the company for the year 1930. During the period 1929 and 1930 many new prospective gas fields had been discovered, and the company was acquiring new leases and proving them by actual development. Many of these prospective gas fields were a considerable distance from the pipe line of the company.

During the year 1930 the company drilled ten dry holes on scattered acreage in Oklahoma, Kansas, and one well in Texas, none of which was drilled in the territory now designated as proven area. The testimony before the Commission clearly discloses that the pioneering period is past. The company now has sufficient developed and proven acreage to satisfy all its requirements for many years. The testimony of both the respondents' and the Commission's witnesses is to the effect that in this proven area there is little or no likelihood of encountering a dry hole in the development of this proven territory. (In fact the valuation upon these leases is fixed and based on the supposition of these leases being proven.) It is true that the company does have unproven and undeveloped acreage, but this acreage is in excess of any reasonable reserve which the company need carry for the protection of its consumers

[fol. 182] and is in excess of any reasonable reserve which should be included in the rate base.

We believe that it would be unsound to use a figure based on the experience of the company during a period when it was pioneering in gas discovery and gas development, in territory which we find is not now used or useful for the purpose of supplying its customers. This is supported by the testimony that the company is now abandoning leases, and has during the period covered by this investigation, sold a large block of its acreage which indicated that part of its acreage was obtained in excess of its reserve requirements and for speculative purposes.

Although there was no testimony that there were any dry holes drilled in the year 1931, and although the testimony of all the witnesses disclosed that there is little likelihood of dry holes being encountered in the proven reserves, herein assigned to the company as used and useful, nevertheless, we deem it advisable to make a reasonable allowance for dry-hole expense.

The evidence shows that the cost of drilling a dry hole varies from $3,000 to $21,000 depending upon the area in which the well is drilled. We believed that an allowance of one dry hole per year, based upon an average of these two figures, would be an ample allowance for this account. We therefore find an allowance of $12,000 to be reasonable.

Annual Requirements for Depletion of Producing Leases

The respondents asked for an annual allowance of $70,569.88 for depletion of producing leases.

The company has arrived at this figure by using the estimated life of the various fields, and the rate at which they are being depleted. We find this to be a reasonable allowance.

We, therefore, find the reasonable allowance for annual reserve requirements pertaining to gas leases to be $83,569. This total added to the average annual depreciation and depletion requirements pertaining to physical equipment other than gas leases in the amount of $1,702,764, gives a total requirement of $1,786,333, which we find to be a reasonable average annual allowance for the periods covered by this investigation.

[fol. 183] Net Earnings of Company Available for Annual Return and the Return Earned

Average Value During Period Covered by Earning Statement

The valuation of the properties of the pipe-line companies were made on behalf of both the companies and the engineering department of the Commission as of September 1, 1931. There should be included in the valuations only properties used and useful in rendering service.

The exhibits introduced relating to income and expenses and net income for the purpose of comparing such net income with the value to determine the rate of return being earned cover principally the calendar year 1930 and the twelve months' period ending June 30, 1931. About the close of the hearing, the company introduced exhibit 92, consisting of one single typewritten sheet which purported to show the net income during the calendar year 1931.

It is obvious that a comparison of net income during 1930 with the value of property used and useful as of September 1, 1931, would furnish no indication of the net return earned during 1930 on the value of the property used and useful during that year, as large additions were made to the property currently during all of that period as well as during the period from December 31, 1930, to September 1, 1931. It must be presumed that additions to the properties were made for the purpose of securing additional revenue or bringing about economies in expenses.

In determining the return earned on property used and useful during 1930, the value of the property used and useful during that period must be found. The only evidence from which such finding may be made consists of the value at September 1, 1931, as testified to by the engineers, and the cost of the net additions from January 1, 1930, to September 1, 1931, as shown by the books and records of the company. In the absence of any very radical change in price levels during the period mentioned, the actual cost of the net additions should compare with the value of such additions at September 1, 1931. Therefore the value of the property used and useful during 1930, which produced the net income earned during 1930, may be fairly ascertained by deducting from the value at September 1, 1931,

the net additions from January 1, 1930, to September 1, 1931, and adding thereto the average additions during the year 1930.

The average additions should be given consideration because obviously additions made during December, 1930, [fol. 184] are not related to earnings during January, 1930, and the additions made during December should be included for one-twelfth of the year, while the additions made in January should be included for twelve-twelfths of a year and the same principle applied to additions during other months.

The cost of reproduction new, exclusive of gas leases, at September 1, 1931, as found herein, is $78,052,486. The cost of reproduction new during the annual periods ending December 31, 1930, and June 30, 1931, has been estimated as follows:

Cost of reproduction new September 1, 1931	$78,052,486
Deduct net additions to fixed capital, July 1, 1931, to September 1, 1931 (Ex. 91)	1,362,506
Cost of reproduction new July 1, 1931	$76,689,980
Deduct net additions January 1, 1931, to June 30, 1931 (Ex. 51)	777,591
Cost of reproduction new January 1, 1931	$75,890,389
Deduct net additions July 1, 1930, to December 31, 1930 (Ex. 51)	10,471,653
Cost of reproduction new July 1, 1930	$65,440,736
Deduct net additions January 1, 1930, to June 30, 1930 (Ex. 51)	592,021
Cost of reproduction new January 1, 1930	$64,848,715

Applying the same per cent condition (89.94) as we found at September 1, 1931, to each of the above reproduction costs results in the following cost of reproduction new less depreciation:

September 1, 1931	$70,199,323
July 1, 1931	68,977,181
January 1, 1931	68,277,816
July 1, 1930	58,859,611
January 1, 1930	58,327,147

The average values found by adding the values at the beginning and end of each period and dividing this total by two follow:

Year ended December 31, 1930	$63,302,482
Year ended June 30, 1931	63,918,396

To which should be added $2,874,390 for the value of the gas leases, which results in average rate bases for the periods of—

Year ended December 31, 1930	$66,176,872
Year ended June 30, 1931	66,792,786

Reducing these values to an average figure, we find the average value for the periods covered by the investigation to be $66,484,829.

Net Income

For the purpose of arriving at the pipe line company's income two annual periods were used in the investigation.

The net income resulting from the operations of the pipe line system during two annual periods ended December 31, [fol. 185] 1931, and June 30, 1931, respectively, follows:

	1930	1931
Net income (Ex. 49, p. 7) before depreciation and depletion	$8,829,480 71	$8,741,899 14
Add:		
Payments to Henry L. Doherty & Co. at rate of 1¾ per cent	75,022 33	68,882 05
Adjustment of federal income tax accrual credited to surplus (Ex. 49, p. 8)	23,310 00	
Construction credit (Ex. 92)	78,874 00	78,874 00
Adjusted net income before depreciation and depletion	$9,006,687 04	$8,889,565 19

The item of 1¾ per cent payments and the reasons it should be disallowed as an item of expense are discussed elsewhere herein.

The adjustment of federal income tax accrual represents a reduction of taxes as stated in expenses.

This adjustment represents the amount charged to expense in anticipation of the federal income tax over and above the amount actually paid.

The construction credit does not appear in the statement of income and expenses covering the periods ended December 31, 1930, and June 30, 1931, but it is shown on ex-

hibit 92, which purports to set forth the expenses during the year ended December 31, 1931. This item of $78,874 represents a reduction in expenses and a like addition to fixed capital representing a proportion of expenses due to construction activities. Those items which appear in expenses include general and administrative expenses, such as salaries and expenses of officials and office employees, legal expenses, rent and some general development expenses, which were charged currently to expenses. At the end of 1931, it appears that a portion of such expenses were found to be attributed to construction activities and portions so found added to fixed capital accounts and expenses correspondingly reduced. The manner in which the amount of expenses charged to fixed capital accounts was determined does not appear in the record. No similar adjustments appears during the periods ended December 31, 1930, and June 30, 1931, and as a large amount of construction was carried on during those periods allowances should be made by reducing expenses, just as they were reduced on exhibit 92. No testimony appearing as to the exact amount which should be deducted it is reasonable to presume that the construction credit should at least equal the credit during 1931; and we have therefore made such adjustment in arriving at net income above.

By averaging the adjusted net income before depreciation and depletion for the two annual periods, December 31, 1930, and June 30, 1931, we find an average annual income of $8,948,126.11 for the periods covered by the investigation. Deducting from this amount the allowance for depreciation, depletion and lease rentals in the amount of [fol. 186] $1,786,333, we find the average annual net income of the company available for return in the amount of $7,161,793, during the periods covered by the investigation.

Average Return Earned During Annual Periods Covered By Investigation

At the beginning of this investigation, the Commission directed that income during at least two annual periods be included in order to eliminate any abnormal fluctuations which might occur and to get a better picture of the average business conditions of the company affecting the gate rate contract. It is the belief of the Commission that rates

should be based on contemplated average conditions over a reasonable period of time. The Commission realizes that the reasonableness of the contract should not be affected and that the contract should not be changed with every minor change in values and costs and minor fluctuation in business conditions.

At the suggestion of the company, the two periods used was the year ending December 31, 1930, and the annual period ending June 30, 1931. The Commission has, therefore, based all its findings on the average of those two periods.

Counsel for the respondents in their reply brief, suggest that the Commission should disregard these periods, or as they state, not "hold the company to the experience of prosperous years."

It appears to be their contention that the Commission should be guided largely by decreased earnings set out in their reply brief which have occurred since the hearing closed. This we do not believe to be proper. The Commission realizes that it is fixing rates for the future and not for the past, but it does not believe that it should be influenced too greatly by decreased earnings occurring over a short period, which can hardly be expected to last indefinitely into the future. In fixing a rate for the future based on past and present conditions, the Commission believes it should give consideration to the present decrease in earnings, and such decrease will be recognized in our conclusion and adjustment of the contract.

From our previous calculations, we have found a present average value of the pipe-line property over two annual periods covered by the investigation to be $66,484,829. We have found the average net income of the company available for return during the same periods to be $7,161,793. This gives an average return earned during the annual periods covered by the investigation of 10.77 per cent.

The Commission is of the opinion that a net return of [fol. 187] approximately 11 per cent is unreasonable at the present time, and was unreasonable during the periods covered by the investigation. It is the opinion of the Commission that no company, dealing at arm's length with an independent company should expect to enter into a contract under conditions such as existed during 1930 and 1931, or up to the present time, by which they would make a net return of 10.77 per cent in a gas pipe-line business.

The Commission appreciates the fact that it is not fixing a definite rate, but in so far as the reasonableness of this contract is to be tested by what it costs the pipe line company to render service, and the rate of return earned, it will be necessary for the Commission to find what is a reasonable return for the pipe line company under present conditions by which to test the reasonableness of the contract.

Fair Rate of Return

In considering what is a fair rate of return to be earned by the pipe line company as a test of the reasonableness of the gate rate contract, the Commission has necessarily taken into consideration what the utility must earn in the light of its situation, its requirements and its opportunities. In dealing with its affiliated distributing companies the Commission has considered the fact that the company should be allowed to earn on the value of its property employed in serving the public with its pipe line, an amount equal to that generally being made by the same business undertakings, which are attended by the same risks and uncertainties. The Commission has also given consideration to the fact that the utilities should be allowed to earn an amount reasonably sufficient to assure confidence in its financial ability and has also considered the amount of risk involved in the pipe line business.

Witness for the respondents testified that an eight per cent return is the usual allowance for public utilities. Other testimony placed the rate of return from six to eight per cent. Practically all of the witnesses agreed that some consideration should be given to the fact that this company was not an ordinary public utility company, but one of a part of a large system organized for the purpose of maintaining the credit of the constituent companies and securing financial assistance. As to just what reduction should be made in the rate of return because of this factor was not stated. To this testimony the Commission must give its own independent consideration in connection with the principles laid down above.

[fol. 188] The testimony was to the effect that because of the assistance of the holding company, the Cities Service Company, the Cities Service Gas Company is and has been able to sell its securities at an "interest rate that was from a half to three-fourths per cent less than anything else that

was put out at about that time on a similar project," and in addition that it gets better terms on its mortgages. It does not have to pay them off in ten years as many of the pipe-line companies have had to do with issues that have been put out in the last two years. Because of this, the Cities Service Gas Company was able to sell its 5½ per cent bonds for 96¼.

"The company having ample financial resources does not necessarily have to issue securities now or six months from now or two years from now. They pick and choose their time when the markets are right."

Page 30, exhibit 49, shows that the company actually sold twelve million dollars of first mortgage, pipe line six per cent gold bonds of the Cities Service Gas Pipe Line Company at par.

It would, therefore, appear that the company is able to obtain funds at a very low rate and is assured of financial stability and a supported credit which enables it to raise the money for the proper discharge of its duties at a very low rate of interest.

It would also appear from the record that there is little risk or hazard in the business of the Cities Service Gas Company. The pipe-line system which it has established is a permanent fixture for an indefinite period. It has a gas reserve which insures it of a supply of gas lasting well into the future. The territory which it serves is well protected; the company has almost a monopoly on the territory which it serves due to the fact that the distributing units are interrelated companies and it would be economically unsound for another pipe-line company to invade its territory.

We are also confronted with changed conditions affecting opportunities for investments which tends to limit the amount of the return. Annual returns upon capital have materially decreased in the past years. Businesses generally are satisfied with a very low rate of return. All businesses, including that of public utilities, are satisfied with a much less rate of return than they were four or five years ago when annual returns upon capital were unreasonably high. Regulatory bodies and courts generally have recognized this factor.

The Cities Service Gas Company is not an ordinary pub- {fol. 189} lic utility, but one of a large system organized

for the purpose of maintaining the credit of subsidiary companies and assisting them in their finances. The records of the Cities Service Gas Company show that it has been able to expand its business so as to meet increased demands, to pay its operating expenses, including interest on money borrowed, to pay dividends of 8 per cent upon its capital stock and accumulate a large surplus. These factors were recognized as material in determining the rate of return in the recent case of Smith v. Illinois Bell Telephone Company, 282 U. S. 159, 191, in which the court said:

"It is evident that in the present case we are not dealing with an ordinary public utility company, but with one that is part of a large system organized for the purpose of maintaining the credit of the constituent companies and securing their efficient and economical management. The record of the Illinois company shows that for many years it has been able to expand its business so as to meet increasing demands, to pay its operating expenses including interest on money borrowed, to pay dividends of 8 per cent upon its capital stock and to accumulate a surplus."

The history of the pipe line under consideration discloses that its operations have been highly successful and enormously profitable. The Cities Service Gas Company was organized in the latter part of 1926, acquiring the assets and assuming liabilities of the following companies:

Empire Natural Gas Company.
Kansas Natural Gas Company.
Empire Gas and Pipe Line Company.
Kansas Oklahoma Gas Company.
Empire Gas and Fuel Company (Delaware). (Gas properties only.)

The stock control of these companies had been theretofore acquired by the Cities Service Company and their assets were acquired and liabilities assumed by the Cities Service Gas Company as of November 30, 1926.

The history of these pipe line companies is a matter of common knowledge and the Commission is familiar with their financial and other operations during the past approximately twenty years. Some of them, if not all, had been in receivership; they had been before the Commission many

times and the Commission had, about 1922 or 1923, acquiesced in the installation of the 40-cent gate rate. The 40-cent gate rate was fixed because it was represented that the companies had been operating at a loss and that there was [fol. 190] an insufficient gas supply.

The effect of the 40-cent gate rate on the financial results of the companies is very clearly illustrated on pages 24 and 25 of Montgomery's exhibit 49. On these pages are set out balance sheets as of November 30, 1926, of the above-named companies, which were consolidated into the Cities Service Gas Company as of November 30, 1926.

These balance sheets show that at the date indicated the book value of the plant investment of the companies, including uncompleted job orders, was $52,182,525.98, and that reserves for depreciation and depletion had been accumulated out of earnings in the amount of $22,423,936.95. These reserves which had been accumulated out of earnings amounted to 42.97 per cent of the plant investment.

These balance sheets further show, notwithstanding the fact that only a few years prior to November 30, 1926, the companies had represented that they had been operating at a loss and proceeded to increase their gate rates to 40 cents, that they had accumulated surplus amounting to $14,903,660.21, which sum is equal to 87.26 per cent of the total capital stock of the companies taken over.

The combined reserves for depreciation and depletion and surplus amounted to $37,327,597.16, which is equal to 218.55 per cent of all outstanding capital stock of the companies and 71.53 per cent of the plant investment.

In the case of the Empire Natural Gas Company, it had a capital stock of $10,574,000, and compared to such capital stock it had surplus of $6,066,436 and reserves for depreciation and depletion of $10,192,715, a total surplus and reserves of $16,259,151, which is equal to 153.77 per cent of its capital stock.

The plant investment of the Empire Natural Gas Company, including uncompleted job orders, as reflected in the books of the company as of November 30, 1926, was $26,577,355; its reserves for depreciation and depletion amounted to $10,192,715, which is equal to 38.35 per cent of the plant investment.

In the case of the Kansas Natural Gas Company it had a capital stock of $6,000,000 and surplus of $7,784,067 and

had accumulated reserves for depreciation and depletion amounting to $11,905,381. Its surplus amounted to 129.73 per cent of its capital stock and the combined surplus and reserves amounted to 198.42 per cent of its capital stock. [fol. 191] The book value of its plant investment was $18,861,223, including uncompleted job orders, and its reserves for depreciation and depletion of $11,905,381 was 63.12 per cent of such plant investment.

The Empire Gas and Pipe Line Company had a capital stock of $5,000 and surplus of $907,323 which was 18,146.46 per cent of its capital stock. Its reserves for depreciation and depletion was $325,840, making the combined reserves and surplus $1,233,163, all of which was accumulated on a capital stock of $5,000.

The plant investment of the Empire Gas and Pipe Line Company, including uncompleted job orders, was $1,625,569 compared with combined surplus and reserves of $1,233,163.

These companies were so prosperous under the 40-cent gate rate during these few years that they were able to loan money to other affiliated companies to the extent of $7,569,571, in addition to paying bond interest and dividends.

Page 23 of exhibit 49 shows what happened when the Cities Service Gas Company was organized and its books opened: $17,080,000 of capital stock and $2,000,000 of bonds became immediately $25,000,000 of common stock and $25,000,000 of 5½ per cent bonds; its reserves for depreciation and depletion became $7,760,706 instead of $22,423,936, as they were before the consolidation. No surplus was carried over into the new Cities Service Gas Company.

The financial history of the company since the consolidation in November, 1926, may be found on pages 1 to 8, inclusive, in exhibit 49, which reflects the combined operations of the Cities Service Gas Company, the Cities Service Gas Pipe Line Company and the American Pipe Line Company.

It is shown there that surplus has been accumulated, in excess of all interest and dividends paid, of $9,044,629 to June 30, 1931; its depreciation and depletion reserves have increased to $10,818,020. Its total assets have increased from $60,595,001 as of December 31, 1926, to $109,431,039 as of June 30, 1931. This enormous increase was accomplished with the addition to the outstanding stock and bonds of only $28,365,700 and loans of $9,000,000. The

company has prospered so that it was able to advance to affiliated companies $2,677,134.

The Cities Service Gas Company has during all this time paid interest on its bonds and dividends on its capital stock; in 1928 it paid $1,000,000 dividends and in 1929 and 1930 it paid $2,000,000 each on dividends, which is at the rate of 8 [fol. 192] per cent per annum. Its earnings before interest were as follows:

1927	$5,385,739
1928	6,053,621
1929	8,060,793
1930	8,829,480
Twelve months ending June 30, 1931	8,741,809

The net profit of the companies, after paying all interest charges, available for reserves and common stock during each of the years 1927 to 1930, was:

1927	14.99%	1929	21.25%
1928	13.12%	1930	19.97%

Its net profit after paying all interest and other charges providing for substantial allowances for depreciation and depletion amounted to the following percentages of its outstanding capital stock during each of the years 1927 to 1930, inclusive:

1927	9.96%	1929	14.53%
1928	6.75%	1930	10.82%

Page 1 of exhibit 49 shows that the plant investment, including uncompleted job orders, increased from $54,243,128 as of December 31, 1926, to $99,003,996 as of June 30, 1931, an increase of $45,760,872. During this period a large line was constructed from Amarillo to Wichita; a line was extended from in the neighborhood of Hutchinson north into Nebraska; lines were extended into Missouri and a great program of expansion carried out. Such program involves large expenditures which affect the operating expenses of the company.

Further, as pipe-line extensions were developed, they necessarily were not fully productive until the volume of sales had been built up to the capacity of such extension. A large proportion of the investment each year was unproductive, although the investment has been included in the

plant investment values included in the above, and will be included in the future. This discussion relative to idle plant is merely for the purpose of illustrating that the company has been earning a high return not only on its production property but on its idle and unproductive property.

During times of higher price levels and when the purchasing power of the dollar was very much less than it is at the present time, eight per cent was generally considered a fair and reasonable rate of return.

The present low level of prices is a matter of common knowledge and the purchasing power of a return of six per [fol. 1931] cent is now greater than the purchasing power of a return of eight per cent was during the periods of higher price levels.

A return of six per cent would not be unreasonable at this time. In fact, the great majority of concerns doing business now are fortunate if they earn as much as six per cent.

We believe that in view of the financial history of this pipe line system, its highly profitable experience, the fact that it is part of a large system with its market assured through affiliated distributing companies, its enormous gas reserves, and all surrounding circumstances, that the maximum rate of return which the Commission should use in determining the reasonableness of the contract is 7 per cent.

System Earning in Excess of a Fair Rate of Return of 7 per Cent During the Annual Periods Covered by the Investigation

The average net income of the company, available for return, during the periods covered by the investigation was $7,161,793, and the average fair value for the same period was $66,484,829. A fair return on the average value at the rate of 7 per cent per annum is $4,653,938, which compared with the net income of $7,161,793 is $2,507,855, in excess of a fair return of 7 per cent.

The gas sold by the company is classified by it as follows:

Domestic:
Main line.
Town-border main line.
Town-border local fields.

Industrial:
Maine line.
Town-border main line.
Town-border local fields.
Drilling and field gas.
Sales to other pipe-line companies.

Main line domestic gas is gas sold from the main line direct to domestic customers.

Town-border main line domestic gas is gas sold from the main line to distributing companies for resale for domestic consumption and these sales are the subject of this investigation.

Town-border local fields gas is gas sold from local fields to nearby distributing companies for resale.

[fol. 194] Industrial gas is gas sold for manufacturing and industrial purposes.

Drilling and field gas is sold in the gas fields for drilling and other purposes.

Sales to other pipe-line companies represents sales to other pipe-line companies who in turn resell it.

The average rates per M. c. f. received from gas sales follows:

Domestic:	1930	1931
Main line	47.2¢	47.0¢
Town-border main line	39.5¢	39.5¢
Town-border local fields	19.3¢	17.3¢
Industrial	15.6¢	15.4¢
Drilling and field gas	18.6¢	18.0¢
Sales to other pipe-line companies	8.4¢	7.4¢
Average (weighted)	23.2¢	23.9¢

Any reduction made as a result of this investigation would affect only the sales of domestic gas from main-line town-border stations.

The sales of domestic gas from main-line town-border stations during 1930 totaled 20,331,209 M. c. f., at the average price of 39.5 cents per M. c. f., producing a total revenue of $8,032,923.

The sale of domestic gas from main-line town-border stations during the annual period ended June 30, 1931, totaled 21,442,841 M. c. f., at the average price of 39.5 cents per M. c. f., producing a total revenue of $8,484,311. The aver-

age annual revenue from main-line town-border domestic gas sales for the periods covered by the investigation was $8,258,617.

The average annual net income from all operations during the periods covered by this investigation, if these domestic sales had been at 30 cents, 32 cents and 35 cents, respectively, would have been as follows:

29½-cent rate	$5,066,848
30-cent rate	5,171,283
32-cent rate	5,589,025
35-cent rate	6,215,634

The Commission, however, appreciates the fact that some consideration must be given to present conditions, which have caused some decrease in the earnings of the company. The Commission also appreciated the fact that it is not fixing a definite rate for the pipe line, but merely using it as a measure to test the reasonableness of the contract.

It therefore appears that if the gate rate were reduced to 29.5 cents, the company would still be making $407,910 in excess of a fair rate of return of 7 per cent on the average value of the property during the periods covered by the investigation.

[fol. 195] The Commission finds that 29.5 cents is a fair and reasonable price to be charged for domestic gas at main-line town-border stations and that anything in excess of 29.5 cents is unreasonable and is not such a contract as parties dealing at arms length under present conditions would enter into.

A 29.5 cent rate for domestic gas for main-line town-border stations results in an average reduction for such gas of 19 cents per M. c. f. A 29.5 cent rate results in an average net income of $407,910 in excess of 7 per cent, which would give the respondents approximately 8 per cent return on the fair value found herein.

At the close of the hearing respondents introduced exhibit 92, which purported to show the loss in earnings after the period covered by the investigation. Although as previously stated, the Commission does not believe that it should test the reasonableness of this contract by an abnormal earning period, but rather on an average period, under average conditions, the Commission realizes that it is de-

termining the reasonableness of the contract for the future and what future conditions may be is somewhat difficult to determine. In view of these conditions the Commission considers that an allowance of a 29.5 cent contract which carries an earning in excess of 7 per cent is liberal.

In their reply brief respondents state that the gross earnings during the first five months of 1932 were several hundred thousand dollars less than the gross earnings for the same period during 1931. Counsel for the Commission suggest that this matter should not be considered as it was not in the record. The Commission feels that they have a general knowledge of the decrease in earnings of all public utilities due to the present depressed condition and that this has been considered by the Commission. In giving consideration to this matter, however, the Commission must also give consideration to other facts of which it has common knowledge. Namely, that the expense of the company has materially decreased with the decrease in gross earnings. The expense of production and transportation of gas is necessarily a big item. In addition, values of all properties have materially decreased. The respondents, in fact, in their last brief, call attention to the fact that salaries and wages of all employees have been recently reduced. It is common knowledge of the Commission that the cost of gas in the fields has been reduced during the past six months. Therefore, decrease in earnings is offset by reduction — expenses.

[fol. 196] Since the beginning of this investigation voluntary reductions in rates have been made at Cherryvale, Newton and El Dorado. Records on file with this Commission, including the orders of the Commission approving the rates, show reductions in the three towns:

Cherryvale on November 5, 1931, was given a new rate of $2.25 for the first 5 M. c. f. as against a previous rate of $3.37 for the first 5 M. c. f., making a reduction of $1.12 for the first 5 M. c. f.

Newton on December 1, 1931, was given a new rate of $3.00 for the first 5 M. c. f., as against a previous rate of $4.75 for the first 5 M. c. f., making a reduction of $1.75 for the first 5 M. c. f.

El Dorado on June 1, 1932, was given a new rate of $2.60 for the first 5 M. c. f., making a reduction of $1.25 for the first 5 M. c. f.

To what extent these reductions affected the earnings of the pipe-line company is not disclosed, but if any reduction in rates were made by the pipe-line company to the operating unit, an order of the Commission reducing the 40-cent charge would not affect the earnings as applied to such sales.

The reduction at El Dorado is of peculiar interest in this investigation, due to the fact that this whole controversy grew out of an attempt to increase the earnings at El Dorado. It is common knowledge that but a short time before the reduction was made at El Dorado the Western Distributing Company, one of the respondents herein, was before the Supreme Court of the United States strenuously contending that the old rate was confiscatory and that the Commission arbitrarily refused to grant an increase of this rate, yet since this contention was made the company has voluntarily reduced their rate.

Respondents in speaking of the decrease in gross earnings in their reply brief, do not disclose whether such decrease is caused by loss in domestic or industrial gas sales: Mr. Montgomery's exhibit 49 shows the revenue from gas sales during the year 1930 and the twelve-months period ended June 30, 1931.

This exhibit shows the domestic sales increased $347,415.85 during the 1931 period compared with 1930, and industrial sales decreased $617,821.98 and field and drilling gas decreased $339,563.58. All of the decrease is in industrial sales and sales other than domestic.

In addition the record shows that the company in 1931 reduced its rate to "other pipe-line companies" from 8.4 cents M. c. f. to 7.4 cents M. c. f., a reduction of over 11 per cent, which indicates that the pipe-line company in dealing with other pipe-line companies recognizes that the cost of producing and delivering gas has decreased.

[fol. 197]

Exhibit 49 further shows that domestic sales increased 686,310 M. c. f. during the 1931 period compared with the 1930 period, and that industrial sales decreased 3,375,194 M. c. f. In so far as the decrease is caused by loss of industrial sales due to temporary abnormal industrial conditions, we do not believe that this additional burden should be placed upon the domestic consumer.

If loss of earnings is due to temporary abnormal industrial conditions it certainly would not be proper to permit

the company to require the domestic business to carry the loss of earnings from the industrial business during the present abnormal period which cannot continue indefinitely into the future. If there is a loss of earnings in this class of business, those rates should be increased to permit that class of business to carry itself.

The Commission also recognizes the fact that the gas company probably has more property in service during the period of 1932 than during the period covered by the investigation. In connection with this, there must also be considered the general decrease in prices which would tend greatly to reduce the valuation of the properties at the present time. To give too serious consideration to these fluctuating conditions would require a reopening of the case and they, no doubt, would be changed before another hearing was completed. The Commission does not believe this to be practical or necessary.

The earnings of 1930 and 1931 were lower as compared to the previous prosperous years, although perhaps not as low as those for 1932, they are no doubt a better measure of the average condition, under which the pipe-line contract must continue. The Commission, therefore, considers in allowing 29.5 cents for town-border main-line gas, that it has reached a fair and equitable result, and that in allowing a return of $407,910 in excess of a 7 per cent return, that they have reached a fair and reasonable conclusion.

The Gate Rate for Cities in Kansas

We have discussed above the return earned by the company from the operation of its entire system. We are concerned with the rates charged in Kansas.

The pipe-line system is used in delivering gas produced and purchased in Texas, Oklahoma, Kansas and Missouri, to purchasers in those states and in Nebraska. The operations of the system are both interstate and intrastate [fol. 198] in Kansas; gas is received from Texas and Oklahoma into Kansas, and gas is produced and purchased and deliveries are made in Kansas and to the states of Nebraska and Missouri.

A determination of a fair gate rate in Texas requires the determination of the value of property located in Texas

and the expenses incident to the operation of that property and an apportionment of such value and expenses to the cost of gas sold in Texas and to the gas delivered from Texas and other states. The same is true as to the gas produced in Oklahoma, Kansas and Missouri.

By finding the value of the property in Texas and the expenses incident thereto and comparing them with the total gas sold in Texas and delivered from Texas to other states the average cost of gas sold in Texas may be arrived at with some degree of approximation and the remainder of the cost would follow the gas delivered to Kansas.

The Commission, in determining that the reasonable gate rate is 29.5 cents, have used that figure in calculating the effect the reduction would have upon all the earnings of the respondents over its entire system. This was necessary in order to get a fair picture of the entire system, but as a matter of fact, the reduction of 11 cents would only apply to the business in Kansas. It might be that a higher rate would be justified in states further distant from the source of supply. Therefore, while we have figured that the 29.5 cent rate would reduce earnings over the entire system, such would not be true unless the same rate were determined to be reasonable in Nebraska, Missouri, Oklahoma, and perhaps Texas.

It is further found, under the authority of chapter 240 of Laws of 1931, that the costs of this proceeding should be taxed against the respondents.

An appropriate order will be issued in accord with the findings in this opinion.

[fol. 198a] ORDER

Now on this 20th day of July, 1932, the above-entitled matter comes regularly before the Commission for final determination and the Commission finds:

1. That the findings in the opinion on the above-entitled matter filed on the 19th day of July, 1932, should be incorporated in this order and made a part hereof.

2. That the distributing companies, respondents above named and the Cities Service Gas Company are mere agents or instrumentalities of the Cities Service Company.

3. That the contract between Henry L. Doherty and Company and the various distributing companies, respondents above named, under which Henry L. Doherty and Company purports to render various departmental services to the distributing companies, and receives as compensation therefor one and three-fourths per cent of the gross revenues of the distributing companies; an engineering fee of five per cent of the cost of construction; a fee for services of the securities department and an additional expense and per diem charge is unreasonable, and that the compensation received thereunder is excessive to the extent of the payment of the one and three-fourths per cent of the gross revenues of the distributing companies, and is not such a contract as parties dealing at arm's length would enter into.

The Commission further finds:

4. That the contract between the Cities Service Gas Company, a natural gas pipe-line company, respondent above named, under which the Cities Service Gas Company sells gas to the distributing companies at the city gate at an average price of 39.5 per M. c. f. is unreasonable, and that the payments made thereunder are excessive in the amount of ten cents per M. c. f. for such main-line border gas.

5. That 29.5 is a reasonable price to be paid to the Cities Service Gas Company by the respondents for main-line town-border gas, and that any amount paid in excess thereof is unreasonable and is not such a contract as parties dealing at arm's length would enter into.

The Commission further finds:

6. That on and after the 1st day of August, 1932, the distributing companies, respondents above named, shall cease to set up on their books as an expense item any pay-
[fol. 198b] ments made to Henry L Doherty and Company under the contract above mentioned, because of the one and three-fourths per cent charge and also any payment made to Cities Service Gas Company for main-line town-border gas in excess of 29½ cents per M. c. f., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

The Commission, therefore, further finds:

7. That on and after the 1st day of August, 1932, that because of the reduction in expense item as above mentioned, the rate to the consumer should be reduced in proportion to the reduction in expenses, pending a final determination of the distributing company rates. Such reduction to be measured by the ten-cent reduction per M c. f. and 1¾ per cent of the gross revenue of the distributing company.

8. That on the 1st day of September, 1932, the distributing companies, respondents above named, shall appear before the Public Service Commission at ten o'clock a. m. for the purpose of showing to the Commission cause why such reductions should not be made permanent and cause why other reductions should not be made as the evidence presented might justify.

The Commission further finds:

9. That the budget department of Henry L. Doherty and Company supervises the transfer of cash to and from New York in accordance with the budget estimates of the Cities Service Company, so that the cash which would otherwise accumulate to the distributing companies is sent on to the fiscal agent in New York to be used for operation and construction programs at other centers, contrary to the statutes of the state of Kansas. (R. S. 17-616.)

10. That under the contract between the Gas Service Company and the various distributing companies, respondents above named, under which the Gas Service Company operates and manages the distributing companies and keeps some of their books and charges to such distributing companies certain sums monthly should not be approved by the Commission because the general ledger and other general books of the distributing companies and practically all of the funds of the distributing companies, pending their transfer to New York, are kept in Kansas City, Mo., contrary to the laws of the state of Kansas. (R. S. 17-616.)

It is, therefore, by the Commission ordered:

1. That on and after the 1st day of August, 1932, the distributing companies, respondents above named, shall [fol. 198c] cease to set up on their books as an expense

item any payments made to Henry L. Doherty and Company under the contract above mentioned, because of the one and three-fourths per cent charge and also any payments made to Cities Service Gas Company for main line town border gas in excess of twenty-nine and one-half cent per M c. f., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

2. That on and after the 1st day of August, 1932, the rate to the consumer shall be reduced by the distributing companies in proportion to the reduction in expenses above named, pending a final determination of the distributing company rates. Such reductions to be measured by the ten-cent reduction per M c. f. and 1¾ per cent of the gross revenue of the distributing companies.

3. That on the 1st day of September, 1932, the distributing companies, respondents above named, shall appear before the Public Service Commission at ten o'clock a. m. for the purpose of showing to the Commission cause why such reductions should not be made permanent and cause why other reductions should not be made as the evidence presented might justify.

By the Commission it is so ordered:

Thurman Hill, Chas. W. Campbell, Commissioners.

Opinion on rehearing omitted here, being identical with Exhibit "K" on page 74 of this record.

Order dated August 31, 1932, omitted here, being identical with Exhibit "M" on page 89 of this record.

Order dated August 31, 1932, omitted here, being identical with Exhibit "M" on page 89 of this record.

[File endorsement omitted.]

[fol. 199] IN UNITED STATES DISTRICT COURT FOR THE DISTRICT OF KANSAS, FIRST DIVISION

In Equity. No. 1646-N

CITIES SERVICE GAS COMPANY, Plaintiff,

against

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, J. W. Greenleaf, Thurman Hill, and Charles W. Camp-

bell, the Persons Constituting the Said Commission, and Roland Boynton, Attorney General of the State of Kansas; The Wichita Gas Company, The Hutchinson Gas Company, The Newton Gas Company, The Pittsburg Gas Company, The Capital Gas & Electric Company, The Wyandotte County Gas Company, The Arkansas Valley Gas Company, The Girard Gas Company, and The Western Distributing Company, Defendants

BILL OF COMPLAINT—Filed Sept. 19, 1932

To said Honorable Court:

Comes now the plaintiff, Cities Service Gas Company, and files this, its bill in equity, and complaining of and against each and all of the above named defendants, respectfully avers:

[fol. 200] I

That the plaintiff is a private corporation duly organized and existing under the laws of the State of Delaware; that it is a citizen, resident and inhabitant of the State of Delaware, with its principal office located in the City of Dover, County of Kent, in said State. The plaintiff, having complied with all of the laws of the State of Kansas governing on the twelfth day of July, 1922, obtained from the Secretary of the State of Kansas a permit to do and transact business in the State of Kansas and that this plaintiff is now and has been ever since July 12, 1922, duly qualified to do business in the State of Kansas.

That the defendant The Wichita Gas Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Wichita, County of Sedgwick, in the State of Kansas.

That the defendant The Hutchinson Gas Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Hutchinson, County of Reno, in the State of Kansas.

That the defendant The Newton Gas Company is a corporation duly organized and existing under the laws of the

State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Newton, County of Harvey, in the State of Kansas.

That the defendant The Pittsburg Gas Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant [fol. 201] of the State of Kansas, with its principal office located in the City of Pittsburg, County of Crawford, in the State of Kansas.

That the defendant The Capital Gas & Electric Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Topeka, County of Shawnee, in the State of Kansas.

That the defendant The Wyandotte County Gas Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Kansas City, Counties of Wyandotte and Johnson, in the State of Kansas.

That the defendant The Arkansas Valley Gas Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Arkansas City, County of Cowley, in the State of Kansas.

That the defendant The Girard Gas Company is a corporation duly organized and existing under the laws of the State of Kansas; that it is a citizen, resident and inhabitant of the State of Kansas, with its principal office located in the City of Girard, County of Crawford, in the State of Kansas.

That the defendant The Western Distributing Company is a corporation duly organized and existing under the laws of the State of West Virginia; that it is a citizen, resident and inhabitant of the State of West Virginia, with its principal office located at Farmers Bank Building, at the corner of Wood Street and Fifth Avenue, in the City of Pittsburgh, County of Allegheny, in the State of Pennsylvania. [fol. 202] The defendant The Western Distributing Company having complied with all of the laws of the State of

Kansas governing, on the thirteenth day of September, 1906, obtained from the Secretary of State of Kansas a permit to do and transact business in the State of Kansas, so that this defendant is now and has been ever since September 13, 1906, duly qualified to do business in the State of Kansas.

The defendant J. W. Greenleaf is a citizen of the State of Kansas, and a resident and inhabitant of the County of Kiowa; that the defendant Thurman Hill is a citizen of the State of Kansas, and a resident and inhabitant of the County of Montgomery; that the defendant Charles W. Campbell is a citizen of the State of Kansas and resident and inhabitant of the County of Norton. That the defendant J. W. Greenleaf is chairman of The Public Service Commission of the State of Kansas, and that the defendants Thurman Hill and Charles W. Campbell are the sole remaining members of the said Commission, and that the last mentioned three defendants are the persons constituting the Public Service Commission of the State of Kansas, which is an administrative body duly created by the statutes of the State of Kansas, and will hereinafter be referred to collectively as the Public Service Commission; that the defendant Roland Boynton is the Attorney General of the State of Kansas, and is a citizen of the State of Kansas and a resident and inhabitant of the County of Lyon.

II

That this is a suit of a civil nature in equity and is brought under the authority of Section 266, as amended, of the Judicial Code of the United States for the purpose of restraining and enjoining, as far as affects this plain- [fol. 203] tiff, the enforcement of two certain orders of the said Public Service Commission dated August 31, 1932 (Exhibits "H" and "I" attached hereto), finding, among other things, that the defendant distributing companies are mere agents or instrumentalities of Cities Service Company, a Delaware corporation, that the contracts between the plaintiff and the defendant distributing companies under which the plaintiff sells gas to the defendant distributing companies respectively at the city gate at an average price of 39.5c per thousand cubic feet are unreasonable, and that the payments made thereunder are

excessive above the amount of 30c per thousand cubic feet for such main line town border gas, that 30c is a reasonable price to be paid the plaintiff by the defendant distributing companies respectively for main line town border gas and that any amount paid in excess thereof is unreasonable, and that on and after the first day of September, 1932, the defendant distributing companies shall cease to set up on their books as an expense item any payment made to the plaintiff for main line town border gas in excess of 30c per thousand cubic feet and should give no consideration to any such payments in fixing a rate for the domestic consumers of the defendant distributing companies, and, among other things, ordering that on and after the first day of September, 1932, the defendant distributing companies shall cease to set up on their books as an expense item any payments made to the plaintiff for main line town border gas in excess of 30c per thousand cubic feet and should give no consideration to any such payments in fixing a rate for the domestic consumers of the defendant distributing companies; and for the purpose of restraining and enjoining each of the defendant distributing companies from failing or refusing to carry out their respective agreements with the plaintiff for the purchase [fol. 204] of natural gas at the city or town border of the various communities served by the defendant distributing companies respectively at the rate, price or charge which each of the said defendant distributing companies has been and is now paying to the plaintiff for such gas, as more particularly stated hereinafter; and is a suit arising under the constitution and laws of the United States, in that, as plaintiff avers, the rate or price that said Public Service Commission directs each of the defendant distributing companies to pay to the plaintiff for natural gas is confiscatory of plaintiff's property used or useful in furnishing service and natural gas to the defendant distributing companies, and said order therefore seeks to deprive plaintiff of its property without due process of law, deny plaintiff the equal protection of the laws, to deny plaintiff freedom of contract and of business, all in violation of its rights under the Fourteenth Amendment to the Constitution of the United States, to impair the obligations of plaintiff's existing contracts in contravention of Article 1, Section 10 of the Constitution of the United States, to contravene Article

1, Section 8 of the Constitution of the United States commonly called the "Commerce Clause" of the said Constitution, all as hereinafter more fully set forth, and therefore said order of the Public Service Commission is null and void. The amount in controversy in this suit exceeds the sum or value of $3,000, exclusive of interest and costs.

III

For some years prior to January 1, 1928, plaintiff owned and operated a system of pipelines and appurtenances located in the States of Oklahoma, Kansas and Missouri, and was engaged in the production, transportation in inter- [fol. 205] state commerce, and the sale of natural gas as a continuous and established business. Additional supplies of gas being necessary for the conduct of business, plaintiff caused to be purchased in the State of Texas and elsewhere gas leases and rights, and caused to be constructed at great expense a pipeline connecting leases and sources of gas supply in the State of Texas and elsewhere to its said pipeline system above referred to, for the purpose of obtaining and transporting in interstate commerce for its present and future markets in Oklahoma, Kansas and Missouri gas owned and controlled by it in the State of Texas and elsewhere.

That from time to time and prior to the second day of July, 1931, plaintiff acquired and now holds and owns, along with other properties, the exclusive gas rights in and to approximately 1,225,000 acres of land situated in the States of Texas, Oklahoma, Kansas and elsewhere, and also as a part of its integrated, interstate pipeline system approximately 4,400 miles of pipelines in said states. That said gas acreage was acquired by the plaintiff in order to insure a dependable supply of natural gas for its customers and also to have dependable gas reserves to meet its future needs, and those of its customers and also to fulfill and carry out its contracts for the sale of gas.

That prior to the second day of July, 1931, plaintiff acquired and now owns, controls and operates an integrated, interstate natural gas pipeline and marketing system located in the States of Texas, Oklahoma, Kansas, Missouri and Nebraska. That plaintiff, by means of its above mentioned pipeline system, transports natural gas

in interstate commerce to various points in said states and delivers same in wholesale quantities to distributing companies, some of which are not affiliated with the plain- [fol. 206] tiff in any way, and also to the distributing companies, defendants in this action, under agreements and contracts lawfully entered into prior to the second day of July, 1931, and the plaintiff also, by means of its said pipeline system, delivers natural gas in wholesale quantities to other purchasers at wholesale under lawful contracts of sale providing for the delivery of such gas, which contracts were made and entered into prior to the second day of July, 1931, and all of which contracts are still in full force and effect.

IV

That plaintiff, prior to July 2, 1931, and relying upon its gas reserves acquired prior to that time for a constant and dependable source of supply, entered into numerous contracts whereby the plaintiff bound and obligated itself to furnish natural gas in wholesale quantities to many gas consumers and to numerous gas distributing companies in cities and towns in the States of Oklahoma, Kansas, Missouri and Nebraska.

That among the contracts so entered into by the plaintiff were contracts with The Wichita Gas Company to supply it with natural gas at the city border of Wichita, Kansas, for distribution to the industries and inhabitants of the said City, with The Hutchinson Gas Company to supply it with natural gas at the city border of Hutchinson, Kansas, for distribution to the industries and inhabitants of the said City, with The Newton Gas Company to supply it with natural gas at the city border of Newton, Kansas, for distribution to the industries and inhabitants of the said City, with The Pittsburg Gas Company to supply it with natural gas at the city border of Pittsburg, Kansas, for distribution to the industries and inhabitants of the said City, with [fol. 207] The Capital Gas & Electric Company to supply it with natural gas at the city border of Topeka, Kansas, for distribution to the industries and inhabitants of the said City, with The Wyandotte County Gas Company to supply it with natural gas at the city border of Kansas City, Kansas, for distribution to the industries and inhabitants of the said City, with The Arkansas Valley Gas Com-

pany to supply it with natural gas at the city border of Arkansas City, Kansas, for distribution to the industries and inhabitants of the said City; with The Girard Gas Company to supply it with natural gas at the city border of Girard, Kansas, for distribution to the industries and inhabitants of the said City, and with The Western Distributing Company to supply it with natural gas at the city borders of twenty-seven towns in the State of Kansas for distribution to the industries and inhabitants of the said cities. That all of the above named companies are defendants in this action (all of such defendants herein being referred to for brevity as the "defendant distributing companies") and distributing companies supplying gas which is furnished to each of them by the plaintiff, which they in turn supply and deliver at retail to domestic consumers in each of said respective cities and towns for heating, lighting and other purposes, and to various manufacturers and industrial plants. That in the nature of things, any interruption, cessation or failure of supply of natural gas will be disastrous to the comfort and health of such domestic consumers and deleterious to the business of those industrial and manufacturing concerns which utilize gas in their operations.

That the plaintiff, for a long time prior to July 2, 1931, and since that time, has been and now is supplying natural gas to each of the defendant distributing companies at the town border of each of the cities and towns served re- [fol. 208] spectively by the defendant distributing companies at a reasonable rate and price under agreements with each of said defendant distributing companies. That the rates or prices at which the plaintiff has been and is now supplying the defendant distributing companies with natural gas as aforesaid are: to The Wichita Gas Company at 40c per thousand cubic feet; to The Hutchinson Gas Company at 40c per thousand cubic feet; to The Newton Gas Company at 40c per thousand cubic feet; to The Pittsburg Gas Company at 38c per thousand cubic feet; to The Capital Gas & Electric Company at 40c per thousand cubic feet; to The Wyandotte County Gas Company at 40c per thousand cubic feet; to The Arkansas Valley Gas Company at 15c per thousand cubic feet; to The Girard Gas Company at 38c per thousand cubic feet; and to The Western Distributing Company at 40c per thousand cubic feet. That

all of the agreements under which the plaintiff has been and now is supplying gas to each of the defendant distributing companies are reasonable and lawful and were entered into by the plaintiff and each of the defendant distributing companies after negotiations looking to the protection of the plaintiff as well as to each of the defendant distributing companies, and after each of the parties thereto had taken into consideration and reflected upon the gas reserves of the plaintiff, the dependability of its source of gas supply and the pipelines and facilities of the plaintiff for properly furnishing the same without interruption.

V

That on or about the second day of July, 1931, the defendants, the said The Public Service Commission of Kansas, J. W. Greenleaf, Thurman Hill and Charles W. Campbell, composing the Public Service Commission of the State of Kansas, all of said defendants being herein referred to as the Public Service Commission, ordered that the reasonableness of all contracts and charges made by holding companies to the defendant distributing companies above named, operating in the State of Kansas, should be inquired into for the purpose of determining the reasonableness of such contracts and the reasonableness of charges made for services and commodities furnished to each of the defendant distributing companies and for that purpose the said Public Service Commission ordered that an investigation be set for hearing on the 18th day of August, 1931, at Topeka, Kansas, to inquire into the reasonableness of contracts made with and services rendered to the defendant distributing companies and other distributing companies, and further ordered that each of the defendant distributing companies appear on the above mentioned date to give to the Public Service Commission such information as they may desire on their own behalf and as may be required by the Commission on behalf of the said investigation and to show cause, among other things, why service or commodity charges made to the defendant distributing companies, including a charge of this plaintiff for the furnishing of natural gas to each of the defendant distributing companies, should such charges be found to be unreasonable, should not be disallowed as operating expenses of the

[fol. 209]

defendant distributing companies, and adjustment made in this respect as to the charges made to the consumers by the defendant distributing companies.

That on the 17th day of August, 1931, said Public Service Commission ordered that such investigation be continued and set for hearing on the 19th day of October, 1931, at the same place.

[fol. 210] That on October 16, 1931, each of the defendant distributing companies filed a special appearance before the said Public Service Commission. Counsel for the defendant distributing companies, in making such a special appearance for each one thereof, made statements, copies of which are attached to this bill of complaint and marked Exhibit "A," which statements set forth the views of counsel for each of the defendant distributing companies as to the nature and extent of the investigation by said Public Service Commission and the special appearance entered on the record.

In these statements, among other things, counsel for the defendant distributing companies stated that each of the defendant distributing companies joined in one order and involved in one hearing are separate and distinct properties serving some 128 cities and communities; that the rates of each system must of necessity be based on the value of its property and its financial experience; that the statutes of Kansas contemplate separate hearings and provide for review of the courts on the record of that property, the venue being determined by the location of the property; that the defendant distributing companies enter said proceeding with the definite contention that it is not a rate case as to any particular property and involves no consideration of the reasonableness or unreasonableness of the rates charged by the defendant distributing companies to their respective consumers; that the most important matter the said Public Service Commission claims a right to investigate is the rate paid for gas by the several distributing companies defendants herein at the city gate, but that the distributing companies would lay all the facts before the said Commission in the said proceeding; that the existing rate charged by the plaintiff for natural gas to be delivered at [fol. 211] the city gate of each of the defendant distributing companies has twice been held reasonable by the courts,

including the highest court of the State of Kansas. Counsel for the defendant distributing companies further stated that the order of the said Public Service Commission dated the second day of July, 1931, seems to contemplate that should the said Commission find forty cents to be too high at the city gate it should be reduced to, say, thirty-five cents or thirty cents; that the reduction of five or ten cents should be adjusted immediately as to each company without a separate hearing as to the needs and requirements of that particular company.

That the hearings in said investigation before said Commission were held from time to time and evidence and exhibits were introduced by the respondent distributing companies in said investigation to show that the contracts between the plaintiff and the defendant distributing companies, the respondents in said investigation before the Public Service Commission, under which the plaintiff sells natural gas to the defendant distributing companies at the city gates for forty cents per thousand cubic feet and in some cases less, were reasonable and such contracts as would be made by perons dealing at arm's length; that the rate or price which the plaintiff charges to the defendant distributing companies at the city gate is fair and reasonable; that the fair value of the property of plaintiff on September 1, 1931, used or useful in its business of supplying natural gas to the defendant distributing companies was $105,857,402 and that its net earnings from operation after depreciation available for the return on said value for the year ending June 30, 1931, was $5,455,032.25, or 5.16% on said return base of $105,857,402, which rate was and is inadequate, unreasonable and confiscatory of plaintiff's property.

[fol. 212] That in the course of the said investigation before the said Public Service Commission each of the defendant distributing companies were prohibited by the said Public Service Commission from introducing any evidence to show the value of the property of each of the said defendant distributing companies used or useful by each thereof in its business of distributing natural gas to the inhabitants of the community which it served and were also prohibited from showing their respective earnings, expenses and their net earnings and the percentage of return which each of the said distributing companies was receiving, based upon

its net earnings and the value of its property used or useful in its business, although each of the said defendant distributing companies asked permission to do so and offered to introduce such evidence for the purpose of showing the rate of return which each of the said defendant distributing companies was making was inadequate, unreasonable and confiscatory.

VI

That on the 20th day of July, 1932, the said Public Service Commission of the State of Kansas handed down its opinion and order dated the 20th day of July, 1932.

That in this order the Commission found that the contracts between the plaintiff and the defendant distributing companies respectively under which the plaintiff sells gas to said defendant distributing companies at the city gates at an average price of 39.5 cents per thousand cubic feet are unreasonable, and that the payments made thereunder are excessive in the amount of 10 cents per thousand cubic feet for such main line town border gas; that 29.5 cents is a reasonable price to be paid the plaintiff by each of the [fol. 213] defendant distributing companies for main line town border gas and that any amount paid in excess thereof is unreasonable and are not such contracts as parties dealing at arm's length would enter into; that on and after the 1st day of August, 1932, defendant distributing companies shall cease to set up on their books as an expense item any payments paid to the plaintiff for main line town border gas in excess of 29.5 cents per thousand cubic feet, and should give no consideration to any such payments in fixing a rate for the domestic consumers of the defendant distributing companies.

VII

That thereafter, and on or about July 30, 1932, each of the defendant distributing companies filed with the said Public Service Commission of the State of Kansas an application for a rehearing, a copy of which (which is the one filed by the defendant distributing company The Arkansas Valley Gas Company) is attached to this bill of complaint and marked Exhibit "B." Each of the defendant distrib-

uting companies filed with the said Commission a similar application for rehearing, properly signed and verified. That in said applications for rehearing each of the defendant distributing companies, fully reserving all their rights as set out in the special appearance contained in Exhibit "A," applied for rehearing in respect to all matters found and ordered by the said Public Service Commission of the State of Kansas, and purported to have been determined by the said Commission for the reason that its decision, findings and order severally and collectively were unlawful, unjust and unreasonable in the respects set forth in said Exhibit "B."

[fol. 214] VIII

That on the first day of August, 1932, the Commission, having before it for consideration the said application for a rehearing, ordered that defendant distributing companies and respondents in said investigation before said Public Service Commission submit to the Commission on or before August 4, 1932, a complete earning and expense statement for the plaintiff covering the year ending June 30, 1932, a copy of which order for information is hereto attached and marked Exhibit "C." That it was recited in the said order that the Commission desired said information in order to enable it to give proper consideration to the application for a rehearing, Exhibit "B," and also in said order said Commission found that information should be included showing to the Commission loss in revenue due to reductions in the price of gas sold by the plaintiff, the amount paid to Henry L. Doherty & Company for the year ending June 30, 1932, and what adjustment was made for construction credit, if any.

That each of the defendant distributing companies and respondents in said investigation before said Public Service Commission on August 4, 1932, filed with the Commission an answer to the said order for information of August 1, 1932, Exhibit "C" similar to the answer filed by the defendant distributing company The Pittsburg Gas Company, copy of which is hereto attached and marked Exhibit "D." That each of the defendant distributing companies in said answer, without recognizing the jurisdiction of the said Commission to issue the said order of August 1, 1932, Ex-

hibit "C," and without waiving their rights to contest the validity thereof, alleged, among other grounds, that under [fol. 215] the statutes of the State of Kansas the proceedings before said Commission were closed by the issuance of its order of July 20, 1932, and that the Commission was without jurisdiction or authority to reopen the same for consideration of further evidence other than by granting respondents' application for rehearing.

That on the fifth day of August, 1932, the said Public Service Commission granted the application of each of the defendant distributing companies respondents in the said investigation before the Public Service Commission and directed that a rehearing be held on the 15th day of August, 1932, at the State House, Topeka, Kansas, at which time the said defendant distributing companies, respondents in the said investigation, would be given an opportunity to present evidence in behalf of their allegations as to the earnings of the plaintiff for the year ending June 30, 1932, and the said Public Service Commission further ordered that its order issued on July 20, 1932, be suspended pending final disposition of the matter after hearing, a copy of which order granting a rehearing is attached to this bill of complaint and marked Exhibit "E."

That thereafter, and on the fifteenth day of August, 1932, a rehearing was held by the said Commission at Topeka, Kansas, at which time each of the defendant distributing companies introduced in evidence an earning statement showing the earnings of the plaintiff for the year ending June 30, 1932.

That at said rehearing each of the defendant distributing companies offered to prove, among other things, that in entering into the contract with the plaintiff for a supply of natural gas to be delivered from plaintiff's main line at the town border of the various communities served by the defendant distributing companies, respectively, each of the [fol. 216] defendant distributing companies were advised of and relied upon the gas reserves of the plaintiff for a constant, dependable supply of gas and offered to show that all of the gas acreage and reserves of the plaintiff were necessary to assure to each of the said defendant distributing companies an adequate and constant supply of natural gas for their needs, and that the pipeline companies obtaining natural gas from the Amarillo field in Texas

were only taking approximately 17% of the gas allowed to be taken from the said field, and the balance of the gas taken from said field is used for gasoline and carbon black plants and the production of oils, or wasted, and the Railroad Commission of the State of Texas has under consideration ordering that all takes of gas from wells be limited to 5% of the open flow of such wells and that all wells having unconnected offset wells be shut down, and that the threatened and contemplated action of the Railroad Commission of the State of Texas, if put into effect this coming winter, would prevent plaintiff from supplying each of the defendant distributing companies with an adequate and dependable supply of natural gas from the Amarillo field, and the plaintiff would necessarily have to draw on its gas reserves in other fields.

That attached to this bill of complaint and marked Exhibit "F" is a copy of said offer of proof presented to the said Public Service Commission at said rehearing by each of the defendant distributing companies herein.

That the said Public Service Commission wrongfully and unlawfully denied to each of the defendant distributing companies the right to make such proof and refused to listen to or permit each of the defendant distributing companies to make any proof whatsoever of the facts offered to be proved before the said Commission by each of the [fol. 117] defendant distributing companies as set forth in Exhibit "F."

That the said Commission only permitted proof of the earnings and expenses and net income of the plaintiff for the year ending June 30, 1932.

IX

That on the 31st day of August, 1932, the said Commission rendered an opinion, a copy of which is attached to this bill of complaint and marked Exhibit "G"; that based upon the said opinion the said Commission issued two orders dated August 31, 1932, copy of which orders are attached to this bill of complaint and marked Exhibits "H" and "I."

That on the 9th day of September, 1932, each of the defendant distributing companies filed with the Public Service Commission of Kansas a second application for re-

hearing, copy of which is annexed to this bill of complaint and marked Exhibit "J."

That thereafter on September 10, 1932, said defendant distributing companies each filed a supplemental application for rehearing, a copy of which is hereto attached marked Exhibit "K" and made a part hereof.

That on the 12th day of September, 1932, the said Public Service Commission entered an order denying said applications for rehearing.

X

That at no time has the plaintiff held itself out as a public utility or common carrier of gas, nor has it at any time engaged in the business of a common carrier. That the entire properties, gas reserves, pipelines and appurte- [fol. 218] nances of the plaintiff have been from the inception of their acquisition by plaintiff and now are devoted exclusively to the plaintiff's private enterprise and business of producing gas from its own properties, transporting the same through its own private pipelines in the states of Texas, Oklahoma, Kansas, Missouri and Nebraska. That plaintiff's gas from the time it begins to move from its position in place within plaintiff's gas lands until the time it is delivered to the defendant distributing companies and others, moves in a continuous and unbroken flow through plaintiff's private pipelines and in interstate commerce. That plaintiff was not and could not have been made a party to said proceeding or investigation before the Public Service Commission of the State of Kansas, did not submit itself to the jurisdiction of the said Commission and therefore has not been afforded or given an opportunity to be heard with respect to the matters and things set forth in this bill of complaint. That the plaintiff's existing contract charges for gas transported in interstate commerce and sold and delivered to each of the defendant distributing companies at the town border of the various communities served by the said defendant distributing companies were in existence prior to the said investigation by said Public Service Commission and were in existence at the date of the said order, Exhibit "H," and that such charges and rates are fair and reasonable.

XI

That the fair and reasonable value of the plaintiff's property used or useful in its business as it existed on the 30th day of June, 1932, is the sum of $105,857,402.00.

That the least fair annual return which the plaintiff is [fol. 219] entitled to earn is an amount equal to not less than eight per cent (8%) of the fair and reasonable value of its property used or useful in the rendition of the services it performs, over and above a proper allowance for replacement reserves. That such a proper annual allowance for replacement reserves should be $3,276,325.07.

That plaintiff's net earnings from operation derived from its said interstate pipeline and gas transportation business for the year ending June 30, 1932, were $7,861,516.85. That after deducting proper annual depreciation allowances of $3,276,325.07 there remains a return upon the fair and reasonable value of the plaintiff's property used or useful in furnishing gas service and exclusively devoted to the rendition thereof for the year ending June 30th, 1932, of four and three tenths (4.3%) per cent.

That the said Public Service Commission in the said investigation found that the value of the plaintiff's property used or useful in its business was only $73,148,510.00 and found that the plaintiff's annual depreciation allowance should be $1,977,591.00. On the said rate base found by the Public Service Commission after deducting therefrom the allowance above set forth, as found by the Commission, the plaintiff would only receive an annual return of 8.04% on the value of its property as erroneously determined by the said Commission. This clearly demonstrates that the contracts which the plaintiff is and has been operating under in selling gas to the defendant distributing companies are not unreasonable but are fair and reasonable, and the rates, charges or prices which the plaintiff makes to the defendant distributing companies for supplying them with natural gas are not excessive or unreasonable, and [fol. 220] that the contracts are such as would have been entered into by persons dealing at arm's length with respect to the same subject-matter.

That the plaintiff's business has been conducted efficiently and economically during all the times herein referred to.

That said opinion and the findings therein contained and the said orders and the findings therein contained, respec-

tively (Exhibits "G," "H" and "I" attached hereto), are unlawful, unjust, unreasonable, confiscatory, void and unconstitutional as respects this plaintiff for, among others, the following reasons:

(a) For the reason that the Public Service Commission, in its investigation of the contracts between plaintiff and the defendant distributing companies for the supply of gas at the city or town borders of the respective communities served by the defendant distributing companies, approached all questions involving the same as if it had power and jurisdiction under the law to fix the rates and commodity charges of the plaintiff and has in effect undertaken to fix the rates and commodity charges of the plaintiff in relation to its interstate business, and the Public Service Commission has undertaken to and has fixed the rates and commodity charges for the plaintiff, and by its decision, opinion, findings and orders (Exhibits "G," "H" and "I" attached hereto) said Public Service Commission has usurped a power to regulate and burden interstate commerce and has acted wholly without constitutional or lawful authority, power or jurisdiction;

(b) For the reason that the gas purchased by the defendant distributing companies, respectively, at the respective town borders of the various communities served by them is natural gas transported by plaintiff in interstate commerce, national in its character, and plaintiff is lawfully [fol. 221] entitled to sell said gas to the several defendant distributing companies herein and to other purchasers in the several states through which plaintiff's transportation system passes without interference by the said Public Service Commission of the State of Kansas or any other state in which said interstate transaction is carried on, and said decision, opinion, findings and orders (Exhibits "G," "H" and "I" attached hereto) unlawfully deprive the plaintiff of the benefits and advantages of its ownership of said gas and said pipeline system and the fruits of its said interstate transportation, and unlawfully deny to the plaintiff the free right to sell from its said transportation system its natural gas so transported, and unlawfully deprives the plaintiff of the rights guaranteed to the plaintiff by Article 1, Section 8, Clause 3, of the Constitution of the United States;

(c) For the reason that the decision, opinion, findings and orders of the Public Service Commission (Exhibits "G," "H" and "I" attached hereto) and each and every part of both thereof, are in violation of Article 1, Section 8, Clause 3, of the Constitution of the United States in that said decision, opinion, findings and orders seek to impose upon the plaintiff an unreasonable regulation and place an undue burden on interstate commerce;

(d) For the reason that the decision, opinion, findings and orders (Exhibits "G," "H" and "I" attached hereto) are in violation of Article 1, Section 10, first subdivision of the Constitution of the United States in that they and each of them impair the obligation of the contracts of the plaintiff with each of the several defendant distributing companies under which each of said defendant distributing companies purchase gas from the plaintiff;

(e) For the reason that said decision, opinion, findings and orders (Exhibits "G," "H" and "I" attached hereto) [fol. 222] are in violation of the Fourteenth Amendment to the Constitution of the United States in that they deprive the plaintiff of its property without due process of law, destroy its freedom of contract and deny to it the equal protection of the laws;

(f) For the reason that the order of the Commission (Exhibit "H" attached hereto) directing that each of the defendant distributing companies shall cease to set up on their books as an expense item any payments made to plaintiff for main line town border gas in excess of 30 cents per thousand cubic feet and shall give no consideration to any such payments in fixing a rate for their domestic consumers, and the findings of the said Commission in the said order that the contracts between the plaintiff and the defendant distributing companies, under which the plaintiff sells gas to the said defendant distributing companies at the city gate at an average of 39.5 cents per thousand cubic feet, are unreasonable and that the payments made under such contracts are excessive above the amount of 30 cents per thousand cubic feet for such main line town border gas supplied to the defendant distributing companies by the plaintiff, fixes a rate, charge or price that would not produce a reasonable return on the fair value of the property

of the plaintiff used or useful in furnishing its interstate gas service to the defendant distributing companies and others, and that if the plaintiff were required to deliver gas to the distributing companies at a rate of 30 cents per thousand cubic feet, it would result in the confiscation of the plaintiff's property and deprive the plaintiff of its property without due process of law, all in violation of the Fourteenth Amendment to the Constitution of the United States;

[fol. 223] (g) For the reason that the plaintiff, in the sale of its said products so transported in interstate commerce, is limited to the market connected with its transportation system, as now located, and that if the said orders of the Public Service Commission (Exhibits "H" and "I" attached hereto) are enforced it will in effect deprive the plaintiff of all market for its gas at rates and charges other than those attempted to be established by the said Public Service Commission in its said decision and orders (Exhibits "G," "H" and "I" attached hereto) and deprive the plaintiff of the right to carry on its business and deprive it of its property without due process of law, all in violation of the Fourteenth Amendment to the Constitution of the United States;

(h) For the reason that said decision, opinion, findings and orders (Exhibits "G," "H" and "I" attached hereto) in so far as they relate to the contracts between the plaintiff and the defendant distributing companies, and under which said defendant distributing companies respectively purchase the supply of gas for distribution to their consumers, impair the operation of such contracts; deny to plaintiff the free right of contract, undertake the business management of the plaintiff; usurp the duties of the officers and directors of the plaintiff and substitute the opinion, judgment and conclusions of the said Public Service Commission for the business opinion and judgment of the officers and directors of the plaintiff as to matters of purely business policy, all in violation of the Constitution of the United States and its amendments;

(i) For the reason that plaintiff has informed and notified each of the defendant distributing companies that plaintiff will not supply said distributing companies with gas at the

rate and charge directed by the Commission in said opinion and order, to-wit: 30 cents per thousand cubic feet at the [fol. 224] city gates of the various communities served by the defendant distributing companies, and if the plaintiff has no other remedy than to do this, such action on its part will undoubtedly result in a multiplicity of suits and in irreparable damage;

(j) For the reason that in the said investigation the said Commission refused to permit the defendant distributing companies to prove that the gas reserves of the plaintiff are all necessary in order to guaranty the fulfillment of the plaintiff's contracts with the defendant distributing companies and to plaintiff's other customers on said system; that the gas reserves of the plaintiff of 71,267 acres allowed by the Commission are inadequate; that said 71,267 acres allowed by the Commission do not contain the gas reserves available to the plaintiff which the Commission found they would have; that during 1931 the total volume of gas taken from the Texas Panhandle gas field was 1,263,000,000 cubic feet per day, of which only 219,000,000 cubic feet per day were taken by the pipelines running into the said field, including that of the plaintiff, or that the pipelines, including that of the plaintiff, only took 17% of the total gas taken from the said Panhandle field; that the gas not taken by pipelines from said field was used by others than the plaintiff in gasoline plants, carbon black plants, production of oils, or blown into the air, and will continue to be so used or wasted in the same proportions unless prohibited by lawful orders of the Railroad Commission of the State of Texas; that said Railroad Commission of the State of Texas has under consideration an order limiting all gas taken from the wells to 5% of the open flow from such wells, and an order shutting in all gas wells having offset wells unconnected with any pipeline; that if the Railroad Commission of the State of Texas makes the proposed order [fol. 225] and it is enforced, the 71,267 acres allowed by the said Public Service Commission of the State of Kansas will be wholly inadequate to supply gas for the needs and requirements of the plaintiff for even the coming winter, and if plaintiff restricts its takes of gas from the said field to the average allowed by the Railroad Commission of the State of Texas its service to the communities in Kansas will

fail; that under present practices in the State of Texas the owners of approximately 10% of the gas leases are producing approximately 82% of the gas produced from the said field, none of which is connected to pipelines, including that of plaintiff, or used by such pipelines; that such practices have reduced the rock pressure in the Borger territory in the State of Texas from the original rock pressure of 430 pounds per square inch to less than 50 pounds per square inch; that gas in the area including the 71,267 acres allowed by the Public Service Commission of the State of Kansas is migrating to the low pressure Borger area; that the reserves of gas under the said 71,267 acres are being thus constantly depleted and are not available to the plaintiff as assumed by the said Public Service Commission of the State of Kansas; that in the computation of the said Public Service Commission of the State of Kansas of proper gas reserves for this plaintiff, said Commission included the open flow of wells sold to the Texoma Natural Gas Company, amounting approximately to 250,000,000 cubic feet per day, which is not available to the plaintiff; that all of these matters should have been taken into consideration in determining the proper gas reserves which the plaintiff is entitled to and which its officers and directors deem proper, and that such matters were not taken into consideration by the said Public Service Commission of the State of Kansas; [fol. 226] that the gas reserves of the plaintiff in all states are not in excess of proper gas reserves as recognized by the gas business and industry and as compared to the gas reserves held by other major pipeline companies, and that none of the gas acreage or reserves now held by the plaintiff was bought or is being held by the plaintiff for speculation or other purpose other than to supply its customers with an adequate supply of natural gas and to fulfill its existing contracts; and that the said Public Service Commission refused to take into consideration the fair market value of all of the plaintiff's gas acreage in determining the value of plaintiff's property used or useful in its business;

(k) For the reason that said decision and orders (Exhibits "G," "H" and "I" attached hereto) are void in that they undertake to put into effect reduced rates and charges for the gas delivered to the defendant distributing

companies by the plaintiff as of September 1, 1932, and that said order is contrary to the statutes of the State of Kansas;

(l) For the reason that said decision and orders (Exhibits "G," "H" and "I" attached hereto) direct an unreasonable, unjust and unlawful discrimination in that said orders direct that gas sold by the plaintiff to the respective defendant distributing companies be sold at a rate different from that plaintiff sells gas to other distributing companies not affiliated with plaintiff;

(m) For the reason that said decision and orders (Exhibits "G," "H" and "I" attached hereto) are the result of the erroneous action of the said the Public Service Commission of the State of Kansas in attempting to average the fair value of the plaintiff's property and earnings over certain periods of time and by its failure to include the value of certain items of property and of certain gas acre-
[fol. 227] age used or useful in the plaintiff's business, and computed plaintiff's earnings on the value of the property allowed by the Commission on a much lower rate base than actually existed, and on which such earnings should have been computed, and that such valuation of plaintiff's property made by the said the Public Service Commission of the State of Kansas is not the fair value of the property of the plaintiff on September 1st, 1931, or on June 30, 1932, and that the earnings of the plaintiff on the erroneous rate base found by the said Commission are not the earnings of the plaintiff as of the thirtieth day of June, 1932, which earnings on the fair value of the plaintiff's property on June 30, 1932, were not in excess of a fair and reasonable return on the fair and reasonable value of its property used or useful in its business, and therefore its contracts with the defendant distributing companies were and are fair and reasonable and such as would have been made by parties dealing at arm's length;

(n) For the reason that the said Public Service Commission unlawfully and unreasonably usurped the prerogatives, duties and authorities of the officers and directors of the plaintiff, upon whom the responsibility for managing the plaintiff and for the plaintiff's service rests, and arbitrarily and unlawfully refused to include in the rate base

of the plaintiff and in the value of its property, leases of the fair market value of many millions of dollars, for the alleged reason that said leases were not, in the opinion of the Commission, presently used or useful and thus the effect will be to deprive the plaintiff of its property without due process of law, contrary to the Constitution of the United States;

(o) For the reason that the said the Public Service Commission of the State of Kansas, in its investigation resulting in the said orders (Exhibits "H" and "I" attached [fol. 228] hereto), eliminated from the operating expenses of plaintiff rentals and charges on gas leases, which leases, in the business judgment of the officers and directors of the plaintiff, are necessary to hold and maintain in order to constitute and insure an adequate, proper and necessary gas reserve for plaintiff's pipeline system to fulfill its contracts and supply its customers with natural gas, and eliminated certain other proper items of expense, thereby unreasonably and unlawfully substituting the said Public Service Commission's opinion for the business judgment of the officers and directors of the plaintiff, in violation of the Fourteenth Amendment to the Constitution of the United States;

(p) For the reason that the said Commission, in its investigation resulting in the said orders (Exhibits "H" and "I" attached hereto), in finding the value of the property of the plaintiff and in allowing replacement reserves, arbitrarily disregarded and ignored testimony and evidence introduced before the said Public Service Commission and uncontradicted with respect to such value and replacement reserves, and thus indirectly deprived the plaintiff of its property without due process of law, in violation of the Constitution of the United States.

(q) For the reason that the said Public Service Commission, in its investigation resulting in said orders (Exhibits "H" and "I" attached hereto), illegally and unlawfully refused to consider or allow certain intangible items of value which should have been allowed in determining the fair value of the property of the plaintiff, upon which the plaintiff was and is entitled to earn a fair and reasonable return;

(r) For the reason that the said Public Service Commission of the State of Kansas has no power or jurisdiction over this plaintiff but that notwithstanding, and in a pro-[fol. 229] ceeding to which this plaintiff was not and could not have been made a party, the said the Public Service Commission of the State of Kansas has made the said orders wherein and whereby this plaintiff is deprived of its rights and properties, and the benefits, advantages and obligations of its contracts without due process of law and in violation of plaintiff's rights under the Constitution of the United States.

XII

That if plaintiff is forced and compelled by reason of the orders of the said Commission (Exhibits "H" and "I" hereto attached) to supply gas to the defendant distributing companies for 30 cents per thousand cubic feet, the compensation it will receive for the said gas will not afford the plaintiff a fair return upon the fair and reasonable value at the time of the use of its property, used or useful in and exclusively devoted to such service, but its return will be confiscatory in effect.

That if the said orders of the Public Service Commission (Exhibits "H" and "I" hereto attached) are enforced against one or more of the defendant distributing companies, such enforcement coercing and compelling each of the defendant distributing companies to violate their respective contracts with the plaintiff for the purchase of gas at the rates now in force by virtue of such contracts, the result will be that by reason of such illegal, unreasonable, unlawful and confiscatory orders and in consequence thereof plaintiff's business and property will be destroyed and the freedom of its interstate business materially interfered with and burdened and its freedom of contract destroyed.

[fol. 230] That the said orders of the said Public Service Commission (Exhibits "H" and "I" hereto attached) are void and in excess of the authority conferred by law upon the said Public Service Commission and further in that said orders deprives the plaintiff of an opportunity to have a judicial determination as to the legality of its contracts and charges to each of the defendant distributing companies by arbitrarily requiring the plaintiff to

reduce its charges for its gas to each of the defendant distributing companies as of September 1, 1932, whether said charges be finally sustained as legal or not; and the said order further on this account seeks to deprive the plaintiff of its property and business without due process of law and deny the plaintiff equal protection of the laws under the Fourteenth Amendment to the Constitution of the United States, and to impair the obligations of its contracts with each of the defendant distributing companies contrary to Section 10 of Article 1 of the Constitution of the United States, and for these reasons said order is null and void.

XIII

That unless the defendants the Public Service Commission of the State of Kansas and members comprising it, are restrained and enjoined as herein prayed, they will, as plaintiff believes and so alleges, attempt to compel the plaintiff and each of the defendant distributing companies, and thus the plaintiff, to comply with the said orders of the Public Service Commission (Exhibits "H" and "I" attached hereto) and to enforce the penalties prescribed by the laws of the State of Kansas for failure to comply with said orders (Exhibits "H" and "I") and the defendant [fol. 231] distributing companies, their respective officers, agents and employees, will be deterred and prevented by the threat of said penalties from carrying out their contracts with plaintiff and from paying to plaintiff the rates and charges which each of the defendant distributing companies have been and are now paying to the plaintiff for natural gas at the town border of the various communities served respectively by the defendant distributing companies and thereby plaintiff will be forced to submit to the confiscation of its property without due process of law and in violation of its rights under the Constitution of the United States as herein alleged, and will be subject to great and irreparable loss and damage.

That plaintiff has heretofore and prior to the thirty-first day of August, 1932, notified the defendant distributing companies that it will not supply them with natural gas except on the basis of the charges and rates in force between the plaintiff and the defendant distributing com-

panies now and prior to the second day of July, 1931, by virtue of the agreements between the plaintiff and the said respective distributing companies; and that for the plaintiff to sell and deliver gas to the defendant distributing companies at the prices fixed by the Public Service Commission in its orders (Exhibits "H" and "I" attached hereto) would not afford the plaintiff a fair and reasonable return on the value of its property used or useful in its business, and would result in the confiscation of its property and business.

XIV

That as further ground for its cause of action plaintiff says that during all the times involved herein, the majority of the voting capital stock of plaintiff has been owned by Empire Gas and Fuel Company, a Delaware corporation. [fol. 232] That of the capital stock of said Empire Gas and Fuel Company a large majority in nominal or par value of said stock is owned by individuals entirely disconnected with Cities Service Gas Company and with Cities Service Company hereinafter mentioned who are citizens of many different states of the Union. These persons own preferred stock of said Empire Gas and Fuel Company to the amount of approximately fifty-four million dollars ($54,000,000.00) in par or nominal value and are entitled to the receipt of profits through dividends before any dividends upon common stock of said Empire Gas and Fuel Company are declared or paid. That Cities Service Company owns a majority of the common stock of said Empire Gas and Fuel Company, and also owns a majority of common stock of Gas Service Company, which latter corporation owns a majority of the common stock of all the distributing companies made defendants herein. That while within the technical provisions of Chapter 239 of the Session Laws of the State of Kansas for 1931, plaintiff is affiliated with each of said distributing company defendants, yet its officers and actual managing agents are for the most part entirely different and the employees of the plaintiff have very little contact with, knowledge of, or acquaintance with the employees of each of said distributing company defendants, and their businesses are for all practical purposes carried on in as independent a manner as if such affiliation did not exist, and the great bulk of the ownership of the Empire

Gas and Fuel Company stock in persons entirely disconnected with any other companies prevents the plaintiff or said distributing companies from being made mere instruments of the other, or the mere instrument of Cities Service Company. That the great majority of stockholders of said [fol. 233] Empire Gas and Fuel Company would receive no benefit whatever from enhanced profits of said distributing company defendants, and the stockholders of said distributing company defendants could not in any wise be benefited by or participate from profits of the plaintiff Cities Service Gas Company. That the said distributing companies, defendants, and this plaintiff have occupied such status with relation to each other during all times involved herein.

XV

That for more than twenty-five years just last passed the plaintiff and its predecessors and grantors have been engaged in the business of transporting natural gas into Kansas from Oklahoma or Texas, or both, as the case may be; that said business passed into the hands of this plaintiff in 1922 and ever since has been and now is owned and operated by plaintiff. That said business during all the time involved herein has been and is now transacted by means of an integrated interstate pipeline system lying in the states of Texas, Oklahoma, Kansas, Missouri and Nebraska, and the same is one integral enterprise and the plaintiff has no other business than that transacted by said integrated system of pipe lines. That in said business, plaintiff has a capital investment of approximately one hundred million dollars. That in the well established course of its said business plaintiff customarily contracts with distributors or other wholesale consumers for the delivery of the gas carried through its said pipeline system before the said gas starts from its place of production in other states, and in order that its said system should effectually and adequately serve the needs of its customers in the State of Kansas, plaintiff has built pipe lines of large capacity and [fol. 234] at proper intervals along the said lines has installed powerful and expensive compressor stations, each composed of many separate power units that may be thrown into or taken out of operation upon a moment's notice to meet the fluctuating demands of its markets, both hourly or

seasonally, and because of the necessity of supporting enormous peaks in times of very cold weather in order that the consumers of its customers might not suffer with cold, it has, because of the consideration that natural gas is a wasting asset, that a given gas field may be unexpectedly and suddenly destroyed by the intrusion of water or other unforeseen disturbances, that the several states have restrictive laws and rules upon the portion of the open flow of a well that may be taken and because of a likelihood of unexpected and radical regulations being at any time imposed by the authorities having jurisdiction of gas conservation in the several states where plaintiff's gas reserves are to control the production from any given field, and other uncertain and hazardous contingencies this plaintiff has been compelled to and in the exercise of its best business judgment has acquired gas leasehold estates of an acreage of approximately 1,225,000 acres in the various states from which it draws its supplies of gas. That plaintiff and its predecessors in said business have already exhausted in the proper conduct of said business which has been a constantly increasing business gas lands of an aggregate area far in excess of the gas reserves it now owns and by reason of such experience plaintiff well knows the necessity of having at all times an adequate reserve and how much reserve is reasonably necessary. That said defendant The Public Service Commission without any knowledge on this subject and without any effort to learn or be informed as to the past experience of plaintiff and its predecessors, [fol. 235] arbitrarily and capriciously substituted its judgment for the judgment of the officers and directors of plaintiff and found that 71,267 acres of gas leases located in Texas, Kansas, Missouri and Oklahoma, was ample and sufficient for plaintiff to adequately supply its customers for a period of twenty-two years, and wrongfully excluded from its valuation of plaintiff's property all other gas leases owned by it. That all of said gas reserve was acquired for the single enterprise composing plaintiff's business and is reasonably necessary to the continuous and dependable operation of the same, and that no person however skilled in the gas industry is able to say for any considerable period in advance at what particular time this plaintiff will be compelled to resort to any given portion of

its said gas reserve for supplying the demands of its customers and meeting the seasonal exigencies of its business.

XVI

That the defendant distributing companies are each and all public service corporations purchasing gas from plaintiff at wholesale at their respective city gates under contract to pay a specified amount, which gas they in turn sell to the inhabitants of the respective cities they serve and their environs. That ever since the year 1911, in which the first public utility law of the state of Kansas was enacted, each of such respective distributing company defendants, during the portion of said period it has been in existence, has been under the jurisdiction and control of the defendant Public Service Commission and its predecessors in office in the usual respects in which Public Service Commissions exercise such control. That the sales to said distributing company defendants constitute the great bulk of plaintiff's business [fol. 236] in the state of Kansas and in practically every instance such defendants have no other source of supply and cannot procure gas elsewhere and also this plaintiff cannot supplant its said customers with other customers for the reason, among others, that its said pipeline system has been built to serve these markets and it is economically prohibitive to lay pipelines to other distant markets even if such markets could be secured. That plaintiff's business could not be continued if it were deprived of the business of said distributing company defendants and in practically every instance the business of said distributing company defendants could not be continued unless they were permitted to purchase gas from plaintiff. That since the enactment of said public utility law as aforesaid and the various successive amendments thereto it has been the subject of litigation as to the extent and application of the powers of the defendant Public Service Commission, and its predecessors in office, which decisions have become and are an integral part of said public utility laws. That among such decisions so supplementing said law there is one by the United States Supreme Court squarely holding as against the predecessors in office of the defendant, Public Service Commission, that the business hereinbefore described and then conducted by a predecessor in title of this plaintiff was an interstate

business of such national concern as to be beyond the jurisdiction of the predecessors in office of the said Public Service Commission and another, by the Supreme Court of the State of Kansas that the present defendant, Public Service Commission, had no power of regulation over this plaintiff which said decisions are equally as integral a part of the public utility laws of the State of Kansas as the text of the law itself, which interpretation and application of said laws has in recent years been uniformly acquiesced in and [fol. 237] accepted by the defendant, Public Service Commission, until the happening of the things complained of herein.

XVII

That according to the usual established course of its business plaintiff has been accustomed to produce or purchase and transport from other states through its said integrated gas pipeline system and sell at wholesale a quantity of gas ranging approximately from a minimum of one hundred million cubic feet daily to a maximum of approximately three hundred thirty million cubic feet daily of natural gas. About 58% of such gas so sold was sold in Kansas and most of that which was sold to domestic consumers in Kansas was and is sold to the distributing company defendants herein. That the prices stipulated in the various contracts with said distributing company defendants vary somewhat because of varying circumstances and conditions but the weighted average price agreed to be paid by said distributing company defendants for domestic gas is 39.5 cents per thousand cubic feet, the maximum price charged to any distributing company defendant being 40 cents per thousand cubic feet. That in each instance the contract was oral and it was agreed and understood that it was to remain in force and effect until changed by agreement of the parties. That said maximum price of 40 cents per thousand cubic feet is the price that was fixed as a reasonable price by the predecessors in office of said defendant Commission for domestic gas in 1923 and is the same price which distributing companies in the state of Kansas entirely unrelated to plaintiff have since paid and still pay to plaintiff and same is a fair and reasonable price for same and the amount necessary for plaintiff to receive in order

[fol. 238] to maintain its said pipeline system and business and produce a moderate and reasonable profit therefrom.

XVIII

That frequently while plaintiff was so conducting its said business it has been compelled to largely expand its facilities to reach other population centers and to render more dependable its service to the distributing companies in the cities which its said pipeline system already reached and as incidental thereto it has been confronted with heavy financing undertakings, construction and managerial problems. That constantly during said period plaintiff has had the advantage of the advice, cooperation, assistance and supervision of many long and widely experienced experts in said respective lines employed by Henry L. Doherty & Company acting as fiscal agent of Cities Service Company, and located in the chief and most advantageous money center of the world, which connection has been extremely valuable and profitable to this plaintiff and has saved it large sums of money as interest and because of its being enabled with such expert assistance to do things most efficiently and to avoid expensive blunders that companies not endowed with such expert and experienced assistance would naturally make in conducting complicated affairs with ordinary employees. That under written contract with said Henry L. Doherty & Company plaintiff has agreed to pay and has in the past paid to said Henry L. Doherty & Company as fiscal agent of said Cities Service Company one and three-fourths per cent of its gross annual income from sales of natural gas to persons and companies other than the distributing company defendants herein and other affiliated companies, such percentage being calculated to recompense [fol. 239] merely said Henry L. Doherty & Company for the actual cost to it of furnishing said services. That said amount averaged over said period has rendered no profit to said Henry L. Doherty & Company but in the aggregate has actually failed to pay to it the actual cost of furnishing said services, and over a period of years said contract has been very advantageous and profitable to this plaintiff. Furthermore during said period since 1927 plaintiff has been able to take from its gas wells located in the Panhandle Field of Texas gas to fill a great portion of its re-

quirements which it produced at small cost to it and at all such times was permitted by the laws and rules of the state of Texas to take from each well a maximum of twenty-five percent of the open flow of such well. That by reason of said advantageous connections and its ability to draw so largely from the Texas Panhandle Field its experience has been fairly profitable and during the year ending with the approximate date of the order hereinafter complained of it made a net profit after depreciation and depletion of approximately five million dollars out of its said business, which constituted a net profit of only about five percent on the value of all the properties owned by it and enlisted in its business. That its gross income for said period was approximately fourteen million dollars and the reduction of its gross income by twenty-five percent would reduce its net income on its investment and the fair value of its properties to approximately two (2%) percent, under which circumstances plaintiff could not continue to operate. That if a reduction be made of its price for domestic gas in Kansas it will be compelled, in order to avoid offensive discrimination and destructive reprisals by other states or their inhabitants, to reduce its prices for such gas in all other states in which it operates.

[fol. 240]

XIX

That while plaintiff was so conducting its well established business in the ordinary way as aforesaid the said defendant The Public Service Commission of the State of Kansas about July 2nd, 1931, and pretending to act under Chapter 239 of the Session Laws of the State of Kansas for 1931, which in substance attempts to confer on said defendant Commission the power to compel holding companies of and corporations affiliated with public utility corporations operating in the State of Kansas to furnish information to it and providing that no management or similar contract of such public utility corporation with an affiliated corporation shall be effective until filed with said Commission, and further providing in substance that upon a proper hearing if such contract be found not to be in the public interest such Commission would be authorized to disapprove such contract, and further providing that "in ascertaining the reasonableness of a rate or charge made by a public utility"

no charge made by a holding or affiliated company shall be given consideration in determining such rate of such public utility to the public unless a showing be made by the utility affected by the charge as to the actual cost to the holding or affiliated company, such showing to consist of an itemized statement furnished by said utility setting out the items, did wrongfully cause to be served upon all of plaintiff's aforesaid customers in the State of Kansas that were directly or indirectly affiliated with it notices of a hearing, a copy of one typical of all of which is hereto attached, marked Exhibit "L" and made a part hereof. That thereafter for more than one year said Commission intermittently held hearings, purporting to be under said notices and wrongfully and without authority of law considered the [fol. 241] aforesaid contract of this plaintiff, which was not a party nor a public utility under the jurisdiction of said defendant Commission, with Henry L. Doherty & Company as fiscal agent of Cities Service Company to pay to it one and three-fourths per cent of its gross receipts from sales of gas to persons and companies not affiliated with plaintiff, and assumed to abrogate and repudiate as a portion of plaintiff's property rights the said contract, whereas neither the statute aforementioned purporting to cover germane matters nor any other statute of the State of Kansas confer upon said defendant Commission the authority or jurisdiction to consider, affect, reject or annul such a contract, it not being one made with a public utility under its jurisdiction. That said defendant Commission, pretending to act under said notice and without ordering or instituting a rate hearing upon any of said distributing company defendants or any other customer of plaintiff to determine the ultimate charge of said customers to the public, wrongfully and without authority of law or any jurisdiction over the subject attempted to impose indirectly upon plaintiff that regulation of plaintiff's business, the direct exercise of which said laws as construed and supplemented by said decisions prohibited to it, and attempted to supersede and supplant the business discretion, judgment and decision of the Board of Directors and officers of plaintiff and of its said affiliated customers, respectively, by unlawfully dictating the purchase price of gas, which was only one element of the ultimate composite sum representing the ultimate charge of

said affiliated customers to the public, thereby depriving this plaintiff and its said customers of the freedom of contract and usurping the power of the Congress of the United States to regulate commerce among the states and depriving plaintiff's said customers, and in necessary effect de- [fol. 242] priving plaintiff, of all corporate autonomy by prohibiting them and it from proportioning the elements entering into the ultimate charge to consumers as the business judgment of said respective customers should dictate, which power said customers legally have and are entitled to exercise constantly so long as they do not exceed such reasonable ultimate rate as the Commission may legally impose, whereas said defendant Commission has no power to consider such things except in a rate hearing, and even in such hearing has no power to determine what a public utility under its jurisdiction shall pay for gas or any other element of its business, but has only the power, and only in such a hearing, to determine and dictate upon proper evidence the ultimate charge of said public utilities to their respective customers. That in such hearing said defendant Commission expressly refused to plaintiff's said customers upon their direct application therefor the right to show, respectively, their present financial experiences so that said defendant Commission might determine for them respectively and appropriate rates to be charged to their customers for the natural gas sold by said customers. That said defendant Commission further wrongfully refused to take or consider plaintiff's well established business as it was currently going forward in the accustomed way or had existed in the recent past or to consider the actual value of the properties acquired for and enlisted in said enterprise, but undertook to revamp the business and select properties of plaintiff, to be considered for the purpose of ascertaining whether plaintiff was earning a reasonable return upon its investment, according to their caprice or inexperienced notions as to what properties only plaintiff ought to own or enlist in such enterprise, and wrongfully undertook to repudiate the aforesaid management contract, not even allowing as an item of expense the quantum meruit of such services, en- [fol. 243] tirely failing and refusing at all times to take the plaintiff, its business, its contracts and profits as they historically existed and were found; but instead insisted upon

considering plaintiff as they pretended to conceive it, its business, its contracts and profits should have been, thereby substituting its business judgment for the business judgment of the plaintiff, although said defendant Commission in substance and effect found that plaintiff was conducting its business in good faith and had wisely acquired and owned many thousand acres of valuable gas lands, which said Commission refused to consider as an integral part of plaintiff's investment in its business or to use as a basis for calculating the percentage of its profits.

XX

That instead of taking plaintiff historically as it found it and attempting to ascertain the actual cost to plaintiff of the commodities it was selling and the service it was furnishing to said distributing companies, said defendant Commission in direct violation of said Chapter 239 and in direct violation of the provisions of the Federal Constitution prohibiting it from regulating interstate commerce, the impairment of contracts, the taking of property without due process of law, rejected the itemized statements of the distributing company defendants herein, showing the cost of the gas and services furnished by plaintiff, without evidence questioning or refuting same, and, as if it had regulatory power over plaintiff, wrongfully and without jurisdiction so to do assumed to take a valuation made by persons selected by said Commission of plaintiff's properties not only in the State of Kansas but also lying in [fol. 244] the States of Texas, Oklahoma, Nebraska and Missouri, where said Commission had no jurisdiction whatever, to determine its reproduction cost new depreciated at the nadir of the trough of the deepest depression the world has ever known, when cost prices were radically below the necessary amounts actually paid by plaintiff and its predecessors in title for construction of its said pipeline system. By this process said defendant Commission eliminated millions of dollars of actual cost and expenditures made by this plaintiff in the lawful conduct of its business; and that by so doing it also excluded from its alleged rate base millions of dollars' worth of leases, thereby in effect confiscating the property of this plaintiff to the extent of such elimination. That plaintiff has no other busi-

ness and unless it is permitted to earn from this business upon all of its property it will be obliged to surrender the leases excluded by said defendant Commission in arriving at its pretended rate base and if the proceeding of said Commission is permitted to stand it will work a confiscation of plaintiff's property to the extent of millions of dollars.

XXI

That in substance the said orders (Exhibits "H" and "I" attached hereto) issued by said defendant Public Service Commission on August 31, 1932, against each and all of the distributing company defendants herein and all other customers of plaintiff in the State of Kansas that are affiliated to it, is that said distributng companies are prohibited from entering upon their books any greater charge for gas sold to them by this plaintiff for domestic use than 30 cents per thousand cubic feet, and from considering in their sales price to their customers any larger amount than said sum, and, contrary to the statutes of Kansas providing [fol. 245] that the orders of the Commission should become effective thirty days after the date of their entry, said defendant Commission directed that its order should become effective the next day following its date, or September 1, 1932. That if said order be permitted to stand and be given force and effect it will prevent said customers of plaintiff from paying to it more than 30 cents per thousand cubic feet for gas sold for domestic purposes, and if said plaintiff is thus wrongfully compelled to sell its product at a price that will constantly cause it loss the inevitable and speedy result will be that its assets will be depleted and its properties destroyed and if on the other hand plaintiff's said customers pay to it the said contract price for domestic gas and are prevented from collecting from their respective consumers more than a rate based upon a purchase price of 30 cents per thousand cubic feet the assets of said customers will be depleted, their respective businesses destroyed and they will become unable to purchase any gas from plaintiff. In either event the necessary effect and operation of said orders will be the destruction of plaintiff's business and the confiscation of its property. That to so destroy plaintiff's said markets as aforesaid by making the orders upon its customers who are necessary

to the continuance of its business will as effectually destroy plaintiff's business and confiscate its property as to make the orders directly upon plaintiff prohibiting it from selling its product for domestic use at more than 30 cents per thousand cubic feet.

XXII

Plaintiff further says that each and all of the distributing company defendants are interested in the subject matter of this controversy and will be compelled to breach their respective gas purchase contracts with the plaintiff [fol. 246] if said orders of said defendant Public Service Commission are permitted to stand, and are proper parties for a complete determination of all the matters involved herein.

XXIII

That the said orders complained of herein violate plaintiff's rights under the Federal Constitution and are in direct contravention of the following provisions of the Constitution of the United States: Clause 1, Section 10, Article 1 of the Constitution of the United States forbidding any state from passing a law impairing the obligation of contracts; the Fourteenth Amendment to the Constitution of the United States forbidding the taking of property without due process of law and the denial of the equal protection of the laws, and Clause 3, Section 8, Article 1 of the Constitution of the United States vesting exclusively in Congress the power to regulate commerce among the states.

XXIV

That the said Public Service Commission, for the purpose of intimidating and coercing this plaintiff and the defendant distributing companies, and by means of such intimidation and coercion preventing the said plaintiff and said defendant distributing companies from seeking any review of the said order of the Public Service Commission (Exhibit "H" attached hereto) in the state courts of Kansas and from seeking any relief by way of injunction or otherwise in this or other courts of the United States, and

by means of such intimidation or coercion of compelling the plaintiff and the defendant distributing companies to acquiesce in and comply with the said order, plans and threatens illegally to institute proceedings in the state [fol. 247] courts of Kansas against the defendant distributing companies in an attempt and with the avowed purpose of having receivers appointed for the defendant distributing companies and through such receivers, if appointed, to have the defendant distributing companies accept and acquiesce in said order and by means of the appointment of such receivers to frustrate and prevent the plaintiff and the defendant distributing companies from seeking or obtaining a review of said order or testing its validity in either the state courts of Kansas of this Court and by such groundless procedure unlawfully to coerce and destroy the plaintiff's customers and prevent such customers of the plaintiff from carrying out or performing their respective contracts with the plaintiff for the purchase of gas, and unlawfully, and by indirect means, to attack and destroy the efficiency, credit and property of this plaintiff and of the defendant distributing companies. That such threatened action, recommendation or purpose on the part of the said Public Service Commission is and would be beyond its power and authority and contrary to the statutes of the State of Kansas, but notwithstanding this it has recommended such procedure to the Governor of Kansas, who in turn has ordered the defendant Attorney General to bring such actions and he has publicly stated that he would speedily do so. That if such proceeding be instituted, irrespective of its final outcome, it would cause this plaintiff irreparable damage and deprive it of its property and contract rights without due process of law and deny to it the equal protection of the laws in violation of the Fourteenth Amendment to the Constitution of the United States, and would impair the obligation of its existing contracts contrary to Section 10 of Article 1 of the Constitution of the United States.

[fol. 248] XXV

Unless the Public Service Commission of the State of Kansas, defendants herein, are restrained and enjoined as herein prayed, as plaintiff believes and so alleges, plain-

tiff's customers will be induced and caused to resist and refuse payment of any charges and rates for natural gas other than those that may result from the enforcement of the said order of the said Commission (Exhibits "H" and "I" hereto attached). Because of the nature of plaintiff's business it has no practical way to enforce the collection of its charges. By cutting off or refusing service for default in the payment of bills rendered, plaintiff's customers, as plaintiff believes and so alleges, will institute large numbers of suits in various jurisdictions throughout the State of Kansas and elsewhere to restrain the plaintiff from cutting off and denying service, and for damages, and also if plaintiff attempts to collect its bills through litigation, such litigation will entail a large number of law suits in various jurisdictions, and therefore plaintiff, in any case, will be subjected to an endless multiplicity of suits. That the issues which would be presented in each such suit are presented and should and will be decided in this action.

XXVI

That Union Public Service Company is a proper but not necessary party and is not made a party for the reason that it cannot be made a party without ousting the jurisdiction on one phase of the case. That plaintiff has no plain, speedy or adequate remedy at law.

Wherefore, plaintiff prays:

1st. That the rate, charge and price of 30c per thousand cubic feet for the defendant distributing companies to pay [fol. 249] to the plaintiff for main line town border domestic gas as prescribed in the orders of the Public Service Commission dated August 31, 1932 (Exhibit "H" attached hereto) be decreed to be confiscatory of the property of this plaintiff, in violation of the Constitution of the United States, and said order imposing the same to be void.

2nd. That The Public Service Commission of the State of Kansas and said individual defendants composing same, and said defendant, Roland Boynton, Attorney General of the State of Kansas, and each of them, their attorneys, agents and employees, and all other persons be temporarily

and permanently restrained and enjoined from any attempt to enforce the said orders of said Public Service Commission or to compel the plaintiff, directly or indirectly, its officers, directors, agents and employees, to comply with, observe or put in force as of September 1, 1932, or comply with, observe or keep in force thereafter the rate, charge or price to the defendant distributing companies or any of them of 30c per thousand cubic feet for main line town border gas supplied to the defendant distributing companies or any of them, or to others, and from any attempt to compel plaintiff, its officers, directors, agents and employees, to comply with or recognize the said orders of the Public Service Commission of the State of Kansas, dated August 31, 1932, (Exhibits "H" and "I" attached hereto) or any other order of the said Public Service Commission, and from taking any steps or proceedings against the said distributing company defendants, their officers, directors, agents or employees, to enforce any penalties or any other remedy for disregarding the rates, charges and prices prescribed by the said orders of the Public Service Commission dated August 31, 1932, (Exhibits "H" and "I" at- [fol. 250] tached hereto) or any of the provisions or findings thereof.

3rd. That the defendant distributing companies and each of them, and all other persons, be temporarily and permanently restrained and enjoined from failing or refusing to carry out their respective agreements with plaintiff for the purchase of natural gas and from failing or refusing to pay to the plaintiff for natural gas received from the plaintiff at the town border of each of the various communities served by the defendant distributing companies respectively the rate, price or charge which each of the said defendant distributing companies has been and now is paying to the plaintiff for such gas, because of said orders or any other orders issued or to be issued out of, based upon or growing out of said proceeding, Docket No. 13127.

4th: That the defendant The Public Service Commission of the State of Kansas, and said individual defendants composing same, and said defendant Roland Boynton, Attorney General of the State of Kansas, and each of them, their officers, agents, servants, employees and attorneys

and those in active concert or participating with them be temporarily and permanently restrained and enjoined from any attempt to bring ouster, dissolution or receivership actions or proceedings against said distributing company defendants or any of them or any other customer of plaintiff in the State of Kansas affiliated with it, for the purpose of preventing disabling or impairing the ability of any or all of them from complying, or to comply, with their said respective contracts with plaintiff hereinbefore set out and from taking any steps that will directly or indirectly bring about or tend to cause such result.

[fol. 251] 5th. That the plaintiff have such other and further relief as may be equitable in the premises.

6th. That a writ of subpoena of the United States of America issue out of and under the seal of this Honorable Court, directed to and against the defendants herein and each of them as required by law, commanding them and each of them on a day certain to be named therein, and under a certain penalty, to appear and fully submit and make answer to this bill of complaint.

7th. That a hearing and determination shall be had herein by three judges as provided by Section 266 of the Judicial Code as amended, for a restraining order and an interlocutory injunction as hereinbefore prayed for, and upon the final hearing and determination upon the merits, and the rendition of final judgment herein, by the said statutory court of three, that a writ of permanent injunction be granted perpetually restraining and enjoining the defendants and each of them as hereinbefore prayed.

And this plaintiff will ever pray.

Cities Service Gas Company, by James W. Finley, Bartlesville, Okla.; R. E. Cullison, Bartlesville, Okla.; Charles A. Frueauff, New York City; Robert S. Sloan, New York City; Fred Robertson, Kansas City, Kan.; J. O. Emerson, Kansas City, Kan, Attorneys for Plaintiff.

[fol. 252] *Duly sworn to by James W. Finley. Jurat omitted in printing.*

Exhibit "A" to Bill of Complaint

Mr. Garver: I desire to make an opening statement to the Commission, and in order that there may be no misunderstanding I have written it.

If the Commission please, at the outset we must confess some uncertainty and confusion as to the nature of this proceeding; the purpose of the Commission; its jurisdiction and our duty. There has never before been anything of the kind attempted and there is no precedent to follow. For this reason and to avoid any uncertainty as to our contentions we have filed written appearances for the several respondents.

[fol. 253] We say the proceeding is unusual in that we have here joined in one order and involved in one hearing separate and distinct properties in some one hundred and eighty cities and communities. Some of these properties have heretofore been involved in separate rate hearings and such hearings as to one property have taken weeks. The rates of each system must of necessity be based on the value of its property and its financial experience. The statutes contemplate separate hearings and provide for a review by the courts on the record as to that property, the venue being determined by the location of the property. It would lead to the utmost confusion, would thwart the purposes of the statute and would jeopardize the statutory and consitutional rights of these several respondents should they be expected to submit to a joint hearing involving the valuation and financial experience of one hundred and eighty properties, none of which is, in any manner, concerned with any other property. We therefore enter this proceeding with the definite contention that it is not a rate case as to any particular property and involves no consideration of the reasonableness or unreasonableness of their rates.

The proceeding, as we recognize it, is an investigation of three particular contracts between companies associated through an ultimate common ownership of a control of their voting stock. These contracts are as follows:

First, the contract with Henry L. Doherty & Company under which 1¾ per cent of the gross earnings are paid to defray the expense, without profit, of services rendered by that organization.

Second, the contract under which the expense of the Gas Service Company is allocated to the several properties, being the expense, without profit, of services rendered by it. [fol. 254] The third is the price paid for gas by the several distributing companies at the city gate.

The first two matters are of slight importance notwithstanding the fact that they have been the subject of much criticism and tirades of abuse. In no rate case so far tried have they been a controlling consideration and they could have been excluded or included without affecting the result of those cases. In the last case involving these properties to be heard by this Commission, El Dorado, we informed the Commission that if not satisfied with the justice of the items they could be thrown out entirely. That is our position now, although we believe they are just and should be so accepted, as they have been so declared by the highest court of our state and by the District Court of the United States. Frankly it has not seemed to us either fair to us or respectful to the courts for this Commission to disregard those decisions and persist in its own contrary judgment. However, we will, in this proceeding, again lay before the Commission all the facts.

As to the city gate rate, the situation is not greatly different although of controlling importance. The existing rate has twice been held reasonable by the courts, including the highest court of this state. Within four months of the last adjudication this Commission dismissed the application of the Western Distributing Company for increased rates at El Dorado because the company declined to again relitigate that matter which the then representatives of this Commission solemnly agreed in open court should be considered as settled. It seemed to us most unfair in that proceeding, which was a hearing in one of twenty-two applications filed by The Western Distributing Company for twenty-two separate towns, some with less than one hundred meters, to expect the distributing company to put on [fol. 255] a complete rate case as to the pipe line. I then informed the Commission such a requirement was prohibitive on account of the expense involved and the smallness of the towns. That this is true is well demonstrated by the expense of this proceeding. At this time of extreme depression, when large industries throughout the country have been compelled to lay off men and cut wages to offset

their greatly reduced earnings in order to survive the crisis, and in the face of a demand of lower rates, we have, to date, in preparation for this proceeding, expended between one hundred fifty and two hundred thousand dollars and the hearing has just begun. This is more than the property at ElDorado ever has or ever will make under its present experience.

In coming before this Commission we do so doubtful of the legal rights of the Commission to compel us to incur this expense doubtful of the legal right to fix an interstate rate in view of many decisions of the United States Supreme Court to the contrary, but realizing a duty to the public to answer our accusers and make all facts public.

We trust this Commission will hear our evidence with open minds and give to us in some measure the benefit of an honesty of purpose. We have naturally been disturbed by articles that have appeared in the press, attributed to members of this body, from which, if true, it would appear the case has been prejudged and its issues determined against us in advance. If so, of course this proceeding is but a farce and an idle gesture. We hope, however, by our conduct in presenting it, to merit your fair and honest consideration.

The majority of this Commission is new to its duties, having taken office within the year. During such time as [fol. 256] the matter of gas rates has been of interest to such members a bitter controversy has existed between our companies and the Kansas City Star involving personal and private differences, and another with the Governor of this State, of a more political nature. Law suits have resulted and charges and counter charges have been made in court and out. It would not be unusual or unnatural if all this had formed a prejudice, consciously or otherwise, in the minds of the public and the minds of the members of this body. I am, therefore, asking that I be indulged in a short history of events that have preceded.

Most of the charges made against us are that we enjoy a monopoly. To the unthinking, monopoly means excess and unjustified profits.

* * * * * * *

Mr. Garver: I think your Commission, in order to give a fair consideration to this matter should know the way

we feel about it. By that I mean our organization, and my clients. There is no malice or animosity in this. I am only getting at this background, as we see it, and try to put yourselves in our position and view the case from that angle.

But this does not follow. At the time Cities Service Company entered the gas business in Kansas the then gas pipe lines enjoyed a perfect monopoly. There were no other companies and they had everything their own way. But they went broke; service failed utterly; the investors lost a large part of their investment; the bankrupt and disgraced properties were sold as is the property of all others who fail.

From the date these failures were purchased and collected into an orderly system service improved and in the past ten years has been such as was never known before [fol. 257] and concerning which there is no complaint now. When these lines were taken over there was no adequate supply of gas—no adequate appliances through which to utilize it. All was confusion as far as the gas business in Kansas was concerned. This has all been changed and to Mr. Doherty more than to any other man, is due the credit for bringing order out of confusion and for rendering service where none before existed.

It has never been the policy of Mr. Doherty to dictate to these properties from an office far distant from their customers, or to place in charge of them men of Wall Street training, unsympathetic with the people served, without understanding of their problems and actuated only by the thought of making money. H. O. Caster is the one now in charge of the natural gas division of Cities Service Company. Judge Caster is a product of a small Kansas town and was formerly attorney for this Commission. He was brought up not in luxury but privation—one of the common people of Kansas, and as much one of them now in his high position as when on the farm in years gone by. No man has ever questioned his word or doubted his integrity. He knows, better than any one else, whether things are right or wrong in Kansas gas rates. He has tried to tell the facts to Kansas officials many times. I doubt if any of them thought he lied but there was always so much political din his voice could not be heard above the tumult. Then there is Jim Finley, formerly one of your judges and

your senator, Sam Hawks, for many years your assistant attorney general; Major Strickler, formerly Chief Engineer of this Commission, myself and many others. Have all these men changed their characters with their employment and sold their birthright for a mess of pottage? I do not believe you have any such thought. As to these men [fol. 258] and myself, we are proud of what has been accomplished by our organization. We feel it has rendered a real service. It is hard for us to realize there is no appreciation of what has been done or to understand the existing criticism.

The rates now in effect are not our arbitrary pronouncements. They have each and all been fixed by either this Commission or by the courts, after repeated and exhaustive investigations and at an expense of many thousands of dollars. We see no reason why these repeated adjudications of our lawful tribunals should be treated with disrespect and in the face of them we should be charged with unlawful conduct. If our system of government is to continue our conduct in the future must be as it has been in the past. There is no other course open to us. When our rates are so established they should be accepted as is the decision of the courts in other matters and the orderly procedure of the courts should not be forgotten and the accusation made that such rates are the offspring of monopoly.

In fact, there is no such thing as monopoly in the gas business regardless of whether there be one company or many. Gas companies are merely merchants selling fuel in competition with other fuels. When the public can buy more comfort and satisfaction for a dollar spent for gas than a dollar spent for coal, oil or electricity, so long and no longer will that dollar be so spent. The competition was never so keen as now. Five years ago the several companies in this group, unable to meet this competition, were losing business steadily year by year. Their revenues were declining so alarmingly that to avoid absolute failure and inability to render service the sale of appliances was undertaken for the sole purpose of increasing the use of this fuel. The result was most satisfactory and the use of gas greatly increased thereby continuing in effect rates [fol. 259] which otherwise would have had to be raised

if the companies were to continue their existence. Now there is an attempt being made to deprive them of the only shield that can protect them against the inroads of their competitors. Instead of monopoly there is competition of the keenest character ever known to the industry.

From the small beginning which our companies made in the purchase of the old Kansas Natural pipe line, a complete, adequate and efficient system, as large as any in the world, has grown. It has not grown by itself nor by reason of earnings of the business. The present value of pipe lines and distribution systems in Texas, Oklahoma, Kansas and Missouri approximates the enormous sum of $150,000,000.00. On this we have never earned a fair return.

But the gas business is only a part of the Cities Service Companies' contribution to the prosperity of Kansas. At this time our affiliated companies have in Kansas 2500 employees, who provide the support for at least 10,000 citizens. The annual salaries and wages to these employees is approximately $3,769,000.00, all of which is spent in Kansas. In addition, our companies in 1930 paid $2,000,000.00 for lease rentals and purchases which went to Kansas farm owners; $1,178,750.00 to Kansas labor; $688,600 to Kansas drilling contractors, most of which went to Kansas labor; $1,148,008.00 was paid to Kansas well-owners for oil; $1,130,000.00 to Kansas well-owners for gas; $1,114,000.00 for 1930 taxes; $1,298,761.00 by gas distribution companies—and other expenditures, the figures for which are not available.

These several known items aggregate $12,327,119.00 spent in Kansas in 1930, more than $1,000,000.00 a month. What other organization in Kansas contributes $1,000,000.00 a month to its prosperity? Our organization feels [fol. 260] that it has done as much for the state as any other organization and fails to understand why it is now singled out for attack.

The intent of Cities Service Company in the beginning was to confine its activities to the pipe line end of the business, leaving the distributing companies in the hands of their then owners entirely unassociated with our organization. Prior to the year 1924 only a few destributing companies of minor importance were owned directly or indirectly by Cities Service Company, the same consisting of the towns in The Western Distributing Company group,

of which El Dorado was the only city of importance. The large markets, such as the two Kansas cities, Wichita, Newton, Hutchinson and Topeka, were owned by corporations unfriendly to the pipeline ownership and had been antagonists in litigation with it for the preceding ten years. There was no co operation on the part of the distributing companies in building up a market which would justify the millions of dollars in additional pipe line investment which was required, not to reach new markets, but to give adequate service to customers then connected. The distributing companies were making no effort to solicit business, were expressly discouraging the use of gas for house heating or industrial purposes and were all experiencing declines in the volume of gas sold and in earnings. In the opinion of the officials of the company, responsible for adequacy of service by the pipe line, the situation was such as to require ownership of the distributing companies in order to assure a market which would justify a greatly increased investment and which was necessary in order to give proper and adequate service to the consumers.

Purchases were made of the distributing company at Topeka, then in the hands of a receiver, and of the dis- [fol. 261] tributing companies at Wichita, Hutchinson, Newton, Pittsburg, the two Kansas Cities, and Union Public Service Company, with distribution systems in some twenty five towns and communities in Kansas, the principal cities being Parsons and Ottawa.

The Gas Service Company was organized in order that experienced and competent men might be placed in close touch with the operation of these properties, it being believed that more could be accomplished by the personal contact of a local organization acting in conjunction and cooperation with the New York office than by that office alone, far distant from the communities' problems.

The agitation against gas companies and the cry of unfairness began at about this time, no doubt due to the fact that the rates fixed in franchises granted by the several cities in the period from 1906 to 1910 had all been set aside as insufficient and confiscatory at the end of years of bitter and expensive litigation and all rates to consumers has been substantially increased.

At the time the properties at Wichita, Hutchinson and Newton were purchased none of them were making oper-

ating expenses and the Kansas Gas & Electric Company had cases pending before the Kansas Commission asking for increases in rates, all of which cases were being bitterly opposed by the several cities. Not desiring to enter said cities as contestants in existing controversies and desiring an opportunity to see what could be done under existing rates; notwithstanding the disastrous experience of its predecessors, the new owners dismissed all said cases then under advisement by the Commission, briefed and ready for decision. The dismissal of these cases did not have the hoped for result and did not lessen the growing agitation.

[fol. 262] Rate cases soon developed on complaints filed by the cities of Wichita, Hutchinson and Newton which resulted in numerous hearings before this Commission, numerous orders and numerous appeals to the courts by the companies involved, the several companies fighting only for a fair return, and contending continually for rates adequate to enable them to render service. Orders issued by the Commission were set aside by the courts and within a few months new orders would be issued by the Commission entirely at variance with the court's decisions. In two instances the Commission did not even wait for appeals from their orders to be determined by the courts in the usual and statutory manner but started new cases involving the same matters for no other purpose than to have the utilities still before them should pending litigation be determined adversely to it.

In addition to rate litigation the several companies in this group were also forced to defend against suits for injunction, suits for receivers, suits to cancel franchises and other litigation, the main purpose of which was to annoy and harass them. All of this litigation was decided in favor of the companies but such decisions, far from being respected, seemed only to have increased the activities of the enemies of our organization and driven them to further and more violent attacks.

As we view this proceeding, the principal issue is as to the reasonableness of the present city gate rate. This rate was established by this Commission in 1923 at a time when the pipe line company submitted itself to the jurisdiction of the Commission and sought its aid in procuring adequate rates. In its order fixing the forty cent city gate

rate this Commission found that the pipe line company in 1923, on the lowest valuation submitted by any of the witnesses, including the Commission's own engineer, was [fol. 263] earning, for return and depreciation, under a thirty-five cent rate, less than two per cent, on such value. Since that time millions of dollars have been spent in the extension of lines to Oklahoma and Texas not for the purpose of seeking additional markets or procuring additional customers but for the purpose of rendering service to the customers then on the system. The valuation which in 1923 was approximately $50,000,000.00, has risen to approximately $100,000,000.00. That money was not procured from the earnings of the system but new and additional capital was required to be advanced by the owners of the property. In the period from 1923 to the present time more money has been invested in additions and betterments than the property has produced for its owners and, as far as the owners of the property are concerned, not one cent has been received in dividends which has not been put back in the property for the benefit of the customers connected therewith. Our organization is likewise unable to understand why its conduct in this regard should not entitle it to some degree of appreciation and approbation rather than continued criticism.

The question in which the Commission should now be interested, and the only issue which we now recognize in this proceeding, as far as the city gate rate is concerned, is as to whether or not the earnings of the Cities Service Gas Company, under the existing city gate rate, are more than a fair return on the fair value of its property. We will show this value, we believe, to the satisfaction of any unprejudiced mind, not only by our own witnesses but by disinterested witnesses of national standing and reputation. In order that the Commission might have in advance a fair opportunity to itself determine the value of this property we have furnished to it not only all the information that has been requested but have granted [fol. 264] access to the books of the respective companies whenever requested and have furnished, without cost to the Commission or its representatives, the cooperation and services of the employees of the respective companies. If there be any question as to that we will leave its answer to Mr. Black and Mr. Montgomery, the engineer and ac-

countant employed by this Commission for the purposes of this proceeding.

On whatever value is shown to exist, the pipe line company is entitled to a fair return. It asks nothing more. At this time it is not receiving such return.

There has always been a tendency on the part of former Commissions to assume the role of operators of utility properties and to substitute their judgment in lieu of the judgment of those entrusted by the owners with this responsibility. This tendency, however, has never been to assume any responsibility for an adequate supply of gas. Over a long period of years the companies have never received any help in this responsibility from regulatory bodies but have always been greatly hampered in their efforts to faithfully discharge their duty by criticism of their judgment and questioning of the reasonableness of their expenditures. The $150,000,000 invested in pipe lines and distribution systems and the $30,000,000 invested by our customers in gas using appliances would be practically lost were it not for an adequate supply of gas at all times, not the present only but indefinitely in the future. Without gas, pipe lines and gas burning appliances become mere junk with no value other than as such. The burden of shouldering this responsibility is no light one and should not be lightly considered either by the public or this Commission.

History has the habit of repeating itself. In the beginning, certain operators thought that gas could be sold at [fol. 265] cheap rates through single barrelled pipe lines built to local fields. When such fields failed the projects failed, the investors lost their money and the public lost service. There always have been and are now those who refuse to profit by experience and who believe, as did the original promoters of the old Kansas Natural, that its original dream can yet be realized. Those experienced in the industry believe that as to all such projects history will again repeat itself.

We know we have an adequate supply of gas for our customers' needs. We do not know that others have. We know we have a system of not one but many lines, not connected to one but many fields. We believe the needs of our customers have been safeguarded by us to the utmost and that we have faithfully performed our duty as to

them. Furthermore, we believe our customers, as a whole, are satisfied both as to service and rates. We know from experience they would prefer present service and present rates to the former inadequate service at lower rates. We respectfully decline to voluntarily do anything to cripple our ability to continue such service; nevertheless we recognize now and always that we are entitled only to a fair return on the fair value of our property. We ask that now nothing more.

* * * * * * * *

Mr. Stone: Now, if the Commission please, the last paragraph of the citation issued by the Commission contains this statement: "It is further by the Commission ordered: That each of the above named respondents appear on the abovementioned date to give to the Commission such information as they may desire on their own behalf, and as may be required by the Commission, in behalf of said investigation, and to show cause why such holding company contracts, or service or commodity charges, should they be [fol. 266] found to be unreasonable should not be disallowed as operating expense of the distributing companies, and adjustment made in this respect as to charges made to the consumers." Now that paragraph, your honors, seems to contemplate that should you find forty cents to be too high at the city gate it should be reduced say to thirty five cents, or thirty cents, that that reduction of five or ten cents should be immediately adjusted as to each distributing company without any separate hearing as to the needs and requirements of that particular company.

* * * * * * * *

Mr. Stone: Our understanding was that the Commission contemplated proceeding then to make such adjustment without any hearing, and that is why we have filed these appearances as to each company, and I will read it so you may understand our position. Maybe there is no difference.

* * * * * * *

Mr. Stone: After stating the appearance, we say:

"Said respondent hereby expressly limits its appearance and appears specially for said purposes and said purposes

only hereby expressly objecting to any consideration by this Commission in this proceeding of the reasonableness or unreasonableness of its existing rates or any attempt to change the same by reason of any findings which this Commission may make in respect to said contracts from the evidence introduced herein and expressly denying the jurisdiction of the Commission to consider in this proceeding any issue as to the value of respondent's property, the adequacy or inadequacy of its earnings or the reasonableness or unreasonableness of its rates for the following reasons:

"1. That the Commission has no jurisdiction, power or [fol. 267] authority, under the laws of the State of Kansas, to proceed against utilities generally in one joint proceeding and to compel one utility to have joined with it others with which it has nothing in common.

"2. That this respondent owns and operates a public utility only in the city of Topeka, Kansas, and its immediate environs and its rates are, by law, required to be determined with respect to the value of its property used and useful in rendering its public service and without regard to the value of the properties of the other utilities joined herein.

"3. That the other parties respondent to this proceeding are improperly joined with the respondent and are not necessary or proper parties as far as any proceeding against this respondent is concerned which involves a consideration of its rates.

"4. That each public utility and each respondent herein as to each property which it operates is entitled under the law, to a full, complete and separate hearing as to each such city or community and the rates as to each such city or community must be considered by this Commission separate and apart and without regard to the property or rates of any other utility.

"5. That it will be impossible, in this proceeding, for any utility to make a record covering proceedings affecting it without including therein proceedings had concerning other utilities and impossible for such utility to avail itself of the right of appeal or review provided by law.

"6. That each utility respondent herein is deprived of the right to conduct its cause according to its independent judgment and in a legal and orderly manner and to avail itself of the rights granted and guaranteed by the Constitution and Laws of the United States and of the State of Kansas.

"7. That the existing rates of this respondent are inadequate, unremunerative and confiscatory in that they do not enable respondent to earn a fair return for all purposes on the fair value of its property and that no change in such rates can lawfully be made without affording respondent an opportunity to present all pertinent facts relating to the value of its property and its financial experience, which opportunity cannot be adequately afforded in this proceeding wherein respondent is joined with utilities operating in some one hundred and eighty towns and communities, the rates for each of which must be determined by considerations entirely independent of every other property."

[fol. 268] EXHIBIT "H" TO BILL OF COMPLAINT

Application for rehearing of The Arkansas Valley Gas Company omitted here, being identical with Exhibit "D" on behalf of The Wichita Gas Company, on page 43 of this record, except verification as follows:

STATE OF MISSOURI,
Jackson County, ss:

Robt. D. Garver, of lawful age, being first duly sworn, says that he is Vice-President of the respondent company filing the foregoing application for rehearing; that he has read over and knows the contents thereof and that the statements of fact therein alleged, and particularly the allegations of fact in paragraph 39 as to the earnings of Cities Service Gas Company for the year ending June 30th, 1932, are true.

Subscribed and sworn to before me this 29th day of July, 1932. My commission expires June 14th, 1934. ——, Notary Public.

[fol. 269] Exhibit "C" to Bill of Complaint

Before the Public Service Commission for the State of Kansas

Docket No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company.

Part A. Wichita Gas Company, Wichita, Kans.;
B. Hutchinson Gas Company, Hutchinson, Kans.;
C. Newton Gas Company, Newton, Kans.;
D. Pittsburg Gas Company, Pittsburg, Kans.;
E. Capital Gas and Electric Company, Topeka, Kans.;
F. Wyandotte County Gas Company, Kansas City, Kans.;
G. Arkansas Valley Gas Company, Arkansas City, Kans.;
H. Girard Gas Company, Girard, Kansas;
I. Union Public Service Company, 45 Towns;
J. Western Distributing Company, 27 Towns;
K. Winfield Natural Gas Company, Winfield, Kan.;
L. Tri-City Gas Company, Kansas City, Mo.;
M. Gas Service Company, Kansas City, Mo.;
N. American Pipe Line Company, Bartlesville, Okla.;
Respondents

[fol. 270] Order for Information in Support of Application for Rehearing

Now on the 1st day of August, 1932, the Commission having before it for consideration the application of the above named respondents for rehearing in the above entitled cause finds:

That in order to enable the Commission to give proper consideration to the application for a rehearing the respondents in support of paragraph 39 of their application should submit to the Commission a complete earning and expense statement for the year ending June 30, 1932.

The Commission further finds that such earning and expense statement should show in detail all the earnings

of the Cities Service Gas Company for the year ending June 30, 1932, and all expense for the same period.

The Commission further finds that information should be included showing to the Commission loss in revenue due to reductions in the price of gas sold by the Cities Service Gas Company, amount paid to Henry L. Doherty & Co. for the year ending June 30, 1932, and what adjustment was made for construction credit if any.

The Commission further finds that the earning and expense statement should be submitted to the Commission on or before the 4th day of August, 1932.

It is, therefore, by the Commission ordered:

That the Respondents submit to the Commission on or before August 4, 1932, a comp. te earning and expense statement for the Cities Service Gas Company covering [fol. 271] the year ending June 30, 1932, in accordance with the findings above set forth.

By the Commission it is so ordered.

Thurman Hill, Chas. W. Campbell, Commissioners.

Attest: Herman L. Gees, Secretary.

EXHIBIT "D" TO BILL OF COMPLAINT

BEFORE THE PUBLIC SERVICE COMMISSION FOR THE STATE OF KANSAS

No. 13127

In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company

Comes now The Pittsburg Gas Company, one of the respondents in the above entitled proceeding, and for its answer to the order of said Commission issued August 1st, 1932, and served upon one of its attorneys at approximately four P. M. on said date, and without recognizing the jurisdiction of the Commission to issue said order, or waiving the right to contest its validity, says:

[fol. 272] 1

That under the Statutes of the State of Kansas the proceedings before said Commission were closed by the is-

suance of its order of July 20th, 1932, and the Commission is without jurisdiction or authority to reopen same for the consideration of further evidence other than by granting respondent's application for a rehearing.

2

That respondent, under the Statutes of the State of Kansas, is entitled to have all evidence introduced by it made a part of the record of said proceedings in such manner that the same may be certified for the purposes of review by the courts, which right it will be denied if the procedure contemplated by said order of August 1st, 1932, is complied with.

3

That the application for a rehearing filed by respondent herein is part of the proceedings for review provided by the Statutes of the State of Kansas, and that Section 6 of Chapter 220, Laws of 1929, expressly prohibits the introduction of the evidence required by the Commission in its order of August 1st, 1932, or any other evidence, and said order of August 1st, 1932, is beyond the jurisdiction or power of the Commission and void.

4

That in said paragraph 39 of its application for a rehearing filed herein on July 30th, 1932, it asked for a rehearing for the reason that conditions had materially changed from those existing at the time of the several hear- [fol. 273] ings herein and that the experience of the Cities Service Gas Company for the year ending June 30th, 1932, was available and would show the ultimate facts set out in said paragraph 39 of said application for a rehearing, which facts are now apparent from an examination of the books of the said Cities Service Gas Company; that in respect to such changed conditions and the said experience of the said Cities Service Gas Company this respondent is entitled to a full and complete hearing and opportunity to present its evidence in the orderly manner contemplated by the Statutes of the State of Kansas and should not and cannot be required to limit its said hearing to the intro-

duction of one exhibit without opportunity to explain the same or in any manner supplement the information asked for by said Commission in said order of August 1st, 1932; that the true situation cannot be presented by any such exhibit even if it were physically possible to prepare the same in the time allowed in said order or within the time allowed by Statute for the consideration of said application and that respondent is unwilling to submit its case in that manner.

5

That even assuming the validity of said order of August 1st, 1932, the engineers and accountants, employed by respondent for the purpose of presenting its evidence and exhibits in said hearings before said Commission and who are familiar with the books and records of the Cities Service Gas Company, are not immediately available and, as respondent is informed and believes, even if present and ready to start the preparation of such an exhibit as is requested by the Commission, could not possibly complete the same in the unreasonably short time allowed by the Commission for that purpose or within the time allowed by [fol. 274] Statute for the consideration of said application for rehearing.

6

That if a rehearing is granted as applied for respondent will show that the amount paid to Henry L. Doherty & Company for the year ending June 30th, 1932, was approximately $52,000.00, representing 1¾ per cent of gross revenues from sales of gas to unaffiliated purchasers, which is a proper charge to the operating expenses of said Cities Service Gas Company for the reason that the prior action of said Commission in disallowing that payment as to the respondent companies was based on the assumption that the services of Henry L. Doherty & Company were duplicated by the services rendered by The Gas Service Company and the fact that respondents were affiliated with Cities Service Company whereas The Gas Service Company renders no services whatever for the Cities Service Gas Company and no possibility of duplication exists and the sales on which such payment is computed are to unaffiliated purchasers exclusively; that even if said item is

eliminated the earnings of the said Cities Service Gas Company would still fall approximately $1,200,000.00 short of a reasonable return had the rate established by said Commission in said order of July 20th, 1932, been in effect and applied to the business transacted by said company for said year ending June 30th, 1932, even if computed upon the Commission's own rate base and the Commission's own rate of return and replacement reserves, all of which is a part of the allowing respondent desires to make on rehearing.

[fol. 275] 7

That if a rehearing is granted respondent will show that during the year ending June 30th, 1932, the price charged by said Cities Service Gas Company to respondents for gas for domestic purposes at the city gates of their respective cities was the same as the price charged during the periods under consideration by the Commission in the previous hearings had herein and no part of the reduction in earnings shown by the experience for the year ending June 30th, 1932, as compared with the earnings for the periods under consideration by the Commission in previous hearings, was due to any such reduction in the city gate rates.

8

It is impossible for respondent to inform the Commission at this time the exact amount of any adjustment for construction credits made during the year ending June 30th, 1932, due to lack of time and opportunity to audit the books of said company for said purpose, but, on rehearing, will show that there was a construction credit of approximately $42,000.00 and that said adjustment was taken into consideration in arriving at the net earnings of $7,865,110.82, as alleged in paragraph 39 of said application for rehearing, and that in arriving at said figure all proper adjustments have been made.

9

Respondent further states that it is impossible to determine whether any part of the decreased earnings of the Cities Service Gas Company was due to a reduction in the price charged for industrial gas without a detailed analysis of every contract of the Cities Service Gas Company and

[fol. 276] of the several respondents herein covering the sale of industrial gas, which detailed analysis it is impossible to make in the time allowed by said Commission or in the time allowed by Statute for the consideration of said application for rehearing.

Wherefore respondent respectfully prays that the rehearing, as applied for, be granted and that it be granted an opportunity to show, in the manner contemplated by the Statutes of the State of Kansas, the several matters alleged in its said application for rehearing.

The Pittsburg Gas Company, by ———, Attorneys.

State of Missouri,
County of Jackson, ss:

H. L. Eastman, of lawful age, being first duly sworn, says that he is the same H. L. Eastman who testified in the hearings had herein as to the valuation and financial experience of the Cities Service Gas Company; that he has personally examined the books of said company for the purpose of ascertaining its financial experience for the year ending June 30th, 1932; that he has read over and knows the contents of the foregoing instrument and that the allegations of fact therein are true.

———

Subscribed and sworn to before me this 3rd day of August, 1932. My commission expires June 14th, 1934. ———, Notary Public.

[fol. 277] Exhibit "E" to Bill of Complaint

Order granting a rehearing omitted here, being identical with Exhibit "E" on page 65 of this record.

Exhibit "F" to Bill of Complaint

Respondents offer to show by the witness A. W. Ambrose that he is Vice President and Assistant General Manager of the Cities Service Gas Company; that he has been with

said Company since the year 1923; that prior thereto he was Chief Petroleum Technologist of the Bureau of Mines of the United States Government; that he is familiar with the gas reserves of Cities Service Gas Company, most of which were purchased under his direction and supervision; that in his opinion as an officer of said company they are all necessary in order to guarantee service to the consumers on said system; that the reserves of 71,267 acres allowed by the Commission are not adequate; that said 71,267 acres do not have the reserves of gas available to Cities Service Gas Company which the Commission found; that during 1931 the total volume of gas taken from the Texas panhandle field was 1,263,000,000 feet per day of which only [fol. 278] 219,000,000 feet per day was taken by pipe lines, or approximately 17 per cent; that the gas not delivered to pipe lines was used in gasoline plants, carbon black plants, the production of oils, or blown in the air and will continue to be so used or wasted in the same proportions unless prohibited by lawful orders of the Texas Commission; that said Commission now has under consideration an order limiting all takes from wells to five (5%) per cent of the open flow and an order shutting in all wells having unconnected offsets; that if the Texas Commission makes the proposed order and it is enforced the 71,267 acres allowed by this Commission will be wholly inadequate for even the coming winter, and if the Cities Service Gas Company restricts its takes to the acreage allowed by this Commission, service will fail; that under present practices in Texas the owners or approximately ten (10%) per cent of the leases are producing approximately eighty two (82%) per cent of the gas, none of which is connected to pipe lines or used by them; that such practices have reduced rock pressure in the Borger territory from the original 430 pounds to less than 50 pounds; that gas in the area including the 71,267 acres allowed by this Commission is migrating to the low pressure Borger area; that the reserves of gas under said 71,267 acres are being thus constantly depleted and are not available to the Cities Service Gas Company as assumed by this Commission; that in its computation of proper reserves this Commission has included the open flow of wells transferred to Texoma amounting to approximately 270,000,000 feet per day; that all of these matters are necessary to be taken into consideration in determining proper re-

serves and were not considered by this Commission as known by it; that the reserves of the Cities Service Gas Company are not in excess of proper reserves as recognized by the gas industry and as owned and held by other major pipe line companies; that none of the gas acreage now held by Cities Service Gas Company was bought or is being held for speculation.

[fol. 279] EXHIBIT "G" TO BILL OF COMPLAINT

Opinion on rehearing omitted here, being identical with Exhibit "K" on page 74 of this record, except as to signatures and dissent of Chairman Greenleaf which were not included in Exhibit "G."

EXHIBIT "H" TO BILL OF COMPLAINT

Order dated August 31, 1932, omitted here, being identical with Exhibit "L" on page 84 of this record.

EXHIBIT "I" TO BILL OF COMPLAINT

Order dated August 31, 1932, omitted here, being identical with Exhibit "M" on page 89 of this record.

EXHIBIT "J" TO BILL OF COMPLAINT

Application for rehearing on opinion and orders omitted here, being identical with Exhibit "N" on behalf of The Wichita Gas Company on page 91 of this record.

EXHIBIT "K" TO BILL OF COMPLAINT

Supplemental application for rehearing on opinion and orders omitted here, being identical with Exhibit "O" on behalf of The Wichita Gas Company, on page 97 of this record.

EXHIBIT "L" TO BILL OF COMPLAINT

Order for investigation omitted here, being identical with Exhibit "A" on page 38 of this record.

[File endorsement omitted.]

[fol. 280] IN UNITED STATES DISTRICT COURT

NOTICE OF HEARING IN CASE NO. 1637-N

To the above-named plaintiff and its attorneys of record:

You and each of you are hereby notified that the Defendants in the above entitled cause will on Saturday, September 24, 1932, at 10 o'clock, A. M., or as soon thereafter as the same may be heard, call up for hearing before a three-judge court, to be assembled by the Honorable Orie L. Phillips in the court room of the Federal Building at Topeka, Kansas, their motion to dismiss the bill of complaint filed by you in the above entitled cause, a copy of which motion is attached hereto.

The Public Service Commission of the State of Kansas, J. W. Greenleaf, Thurman Hill and C. W. Campbell, the Persons Constituting said Commission, Defendants. Chas. Welch, Harry Castor, Chas. W. Steiger, E. H. Hatcher, Attorneys for Defendants.

[fol. 281] IN UNITED STATES DISTRICT COURT

[Title omitted]

MOTION TO DISMISS BILL OF COMPLAINT—Filed Sept. 23, 1932

Come now the undersigned defendants and say:

That said Bill of Complaint ought to be dismissed because it appears upon the face of the bill of complaint:

1. That the bill of complaint does not make out or state such a cause of action as to entitle the plaintiff to the relief prayed for or to any relief.

2. That this court is without jurisdiction to try the cause.

Wherefore Defendants pray that the bill of complaint be dismissed and the costs be taxed to the plaintiff.

The Public Service Commission of the State of Kansas, J. W. Greenleaf, Thurman Hill, and C. W. Campbell, the Persons Constituting the said Commission, Defendants. , Attorneys for Defendants.

[File endorsement omitted.]

[fol. 282] In United States District Court for the District of Kansas, First Division

In Equity. No. 1637-N

The Wichita Gas Company, a Corporation, Plaintiff,

vs.

The Public Service Commission of the State of Kansas, and Jesse W. Greenleaf, Thurman Hill, and C. W. Campbell, as Members of said Commission, and Roland Boynton, Attorney General of the State of Kansas, Defendants

In Equity. No. 1638-N

The Hutchinson Gas Company, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1639 N

The Newton Gas Company, a Corporation, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1641-N

The Capital Gas & Electric Company, a Corporation, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1642 N

THE WYANDOTTE COUNTY GAS COMPANY, a Corporation, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1640 N

THE PITTSBURG GAS COMPANY, a Corporation, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1643 N

THE CHANUTE GAS COMPANY, a Corporation, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1644 N

UNION PUBLIC SERVICE COMPANY, a Corporation, Plaintiff,

vs.

Same, Defendants

In Equity. No. 1645 N

WESTERN DISTRIBUTING COMPANY, a Corporation, Plaintiff,

vs.

Same, Defendants

[fol. 283] ORDER CONSOLIDATING CAUSES NOS. 1637-N TO 1645-N, INC. Filed Sept. 24, 1932

The above entitled causes came on to be heard on this 24th day of September, 1932, before Honorable Orie L. Phillips, Circuit Judge, Honorable George T. McDermott, Circuit Judge, and Honorable Richard J. Hopkins, District Judge; plaintiff in each case appearing by Robert D. Garver and Robert Stone, its counsel, and the defendants The Pub-

lic Service Commission of the State of Kansas, Jesse W. Greenleaf, Thurman Hill and C. W. Campbell, appearing by Earl H. Hatcher, their counsel; and Roland Boynton, Attorney General, appearing by Walter T. Griffin and Everett E. Steerman, his counsel.

It appearing to the court and counsel consenting thereto that the aforesaid cases should be consolidated,

It is hereby ordered, adjudged and decreed that said causes be and they are hereby consolidated for the hearing and for the trial of said causes, and proceedings hereafter may be had and entitled The Wichita Gas Company vs. The Public Service Commission of the State of Kansas et al., being cause No. 1637-N, Consolidated.

It is further ordered, adjudged and decreed that the motion filed by the Attorney General to dismiss as to him is hereby overruled, to which ruling the defendant in open court objected and excepted, which objections and exceptions were made and allowed.

It is further ordered that the motion of the defendants, The Public Service Commission of the State of Kansas, Jesse W. Greenleaf, Thurman Hill and C. W. Campbell, constituting said Commission, to dismiss the bill of complaint be and the same is hereby overruled, to which ruling said defendants in open court objected and excepted and exceptions were duly allowed.

Thereupon the court allowed the defendants and each of them seven (7) days in which to file answers to said causes, [fol. 284] counsel in open court accepting such limitation and consenting to the fixing of that date.

Orie L. Phillips, Circuit Judge. Geo. T. McDermott, Circuit Judge. Richard J. Hopkins, District Judge.

[File endorsement omitted.]

[fol. 285] IN UNITED STATES DISTRICT COURT

ORDER CONSOLIDATING CASE NO. 1646-N WITH CASE NO. 1637-N —Filed Sept. 24, 1932

Now on this 24th day of September, 1932, it is ordered by the Court that the above entitled case be and the same is

hereby consolidated for the hearing and for the trial thereof with the case entitled The Wichita Gas Company vs. The Public Service Commission of the State of Kansas, et al., being cause No. 1637-N, consolidated.

Orie L. Phillips, Circuit Judge. Geo. T. McDermott, Circuit Judge. Richard J. Hopkins, District Judge.

[File endorsement omitted.]

[fol. 286] IN UNITED STATES DISTRICT COURT

[Title omitted]

ANSWER OF DEFENDANTS IN CASE NO. 1637 N FILED OCT. 3, 1932

The joint and several Answer of the Public Service Commission of the State of Kansas, J. W. Greenleaf, Thurman Hill and C. W. Campbell, to the bill of complaint of The Wichita Gas Company, a corporation, plaintiff.

These defendants, now and at all times hereafter saving and reserving to themselves, and each of them, all benefit and advantages of exception, which can or may be had or [fol. 287] taken to the many errors, uncertainties and imperfections in the said plaintiff's bill of complaint contained, for answer thereunto or unto so much and such parts thereof as the defendants are advised is or are material or necessary for them to make answer unto, they, these defendants severally answering, say:

1, 2, 3, 4, and 5

They admit the allegations of paragraphs one, two, three, four and five of the bill of complaint.

6

Said defendants say that they have no such information as will enable them to affirm or deny the allegations in paragraph six that plaintiff has no supply of gas for sale and distribution to its customers other than the supply it purchases from the Cities Service Gas Company at the agreed price of forty (40) cents per thousand cubic feet for domes-

tic gas to plaintiff for a less price and plaintiff has no other source of supply available to it and without its present supply cannot carry on its said business.

These defendants answering further say that while it is true that plaintiff, as a legal entity does not produce or manufacture gas for sale or distribution to its customers, it does, by, thru and in conjunction with its affiliated company, the Cities Service Gas Company, both the plaintiff and the Cities Service Gas Company being subsidiaries [fol. 288] of the Cities Service Company, have control thru its holding company, The Cities Service Company, of a natural gas supply.

7

These defendants deny that the present value of plaintiff's property used and useful in rendering the service in which it is engaged is not less than a sum of $2,872,854.00; and further answering these defendants aver that the value of plaintiff's property devoted to the public purpose in supplying its customers with natural gas is substantially less than the valuation claimed by the plaintiff, and defendants further say that with reasonable and necessary operating expenses paid from the gross revenue of plaintiff's gas distributing plant and with lawful rates complained of in effect the property of plaintiff would net to it a reasonable return upon the fair value of its property.

8

Defendants admit the allegations of paragraph eight, except that they deny that under existing rates the present earnings are inadequate and unreasonable.

9, 10, 11, 12, 13, 14, and 15

Defendants admit the allegations of paragraphs nine, ten, eleven, twelve, thirteen, fourteen and fifteen of plaintiff's bill of complaint, except that the defendants deny that the Commission at any time undertook to order plaintiff to make no payments to the Cities Service Gas Company in excess of 29½ cents per M c. f. as alleged in paragraph twelve.

[fol. 289] Defendants admit that on rehearing on August 15, 1932, plaintiff attempted to introduce other evidence in

connection with other matters assigned and alleged as grounds for rehearing in its application set out in plaintiff's bill of complaint as Exhibit "E," but defendants deny that plaintiff was wrongfully and unlawfully denied the right so to do. Defendants further answering allege that the Commission rightfully restricted the rehearing to the allegations of paragraph thirty-nine of plaintiff's said application, the application being granted as to paragraph thirty-nine only, said proceedings were not open for all purposes of the original hearing.

17

Defendants have no information sufficient to enable them to affirm or deny the allegations of paragraph seventeen of the bill of complaint as to what evidence could be introduced concerning matters other than those alleged in paragraph thirty-nine of plaintiff's said application set out in its bill of complaint as Exhibit "E"; defendants answering further allege that the Commission properly restricted the introduction of evidence to paragraph thirty-nine of plaintiff's application for a rehearing set out in plaintiff's bill of complaint as Exhibit "E."

[fol. 290] 18

Defendants admit the allegations of fact made in paragraph eighteen of plaintiff's bill of complaint, and answering further allege that the year ending June 30, 1932, covered but one of the three test periods used by the Commission, and was not alone a proper measure of the reasonableness of the contract between plaintiff and the Cities Service Gas Company.

19

Defendants deny that in the opinion on rehearing, set out in plaintiff's Exhibit "K," that the Commission found that the Cities Service Gas Company was earning only 8.0438 on the value found by the Commission, and deny that the Commission ignored the fact it had no jurisdiction of the Cities Service Gas Company to fix its rate to be charged in interstate commerce and denies it ignored the fact that it had under consideration only the reasonableness of the contract between the Cities Service Gas Company and the plaintiff

as of the time of said investigation and defendants further deny that the Commission unlawfully and arbitrarily proceeded to find the average value of the Cities Service Gas Company over a three year period and the average depreciation and depletion requirements for the same period. The defendants answering further allege that the Commission properly took the test period covering three years in which to determine the reasonableness of the contract and fixed a price to be charged by the Cities Service Gas Company for gas at thirty (30) cents which would produce a return of approximately 7 per cent on the average value of the Cities Service Gas Company's property.

[fol. 291] Defendants answering further allege that due to the affiliation between the plaintiff and the Cities Service Gas Company, the common stock of both companies being owned indirectly by the Cities Service Company that the reasonableness of the contract was properly measured by a return of approximately 7 per cent to the Cities Service Gas Company on the fair value of its property.

20, 21, 22, and 23

Defendants admit the allegations in paragraphs twenty, twenty-one, twenty-two and twenty-three of plaintiff's bill of complaint.

24

Defendants deny the allegations of paragraph twenty-four of plaintiff's bill of complaint that the order issued by the Commission on August 31, 1932, and set out in plaintiff's bill of complaint as Exhibit "L," in which said Commission finds unreasonable and refuses to recognize the plaintiff's contract to the Cities Service Gas Company for the purchase of its supply of gas at the city gate, its contract with Henry L. Doherty & Company, under which plaintiff pays 1¾ per cent of its gross revenues for services rendered to it by said Henry L. Doherty & Company is unnlawful, unreasonable and void because it is in direct violation of the constitution and laws of the State of Kansas and the constitution of the United States, and defendants answering further allege that said order is lawful and reasonable and [fol. 292] not in violation of the laws of Kansas or the United States. Defendants admit that the order issued by the Commission on August 31, 1932, and set out in plain-

tiff's bill of complaint as Exhibit "M," is unlawful and therefore void under the laws of the State of Kansas.

25

Defendants deny that the orders of the Commission, and each and all of them, in so far as they purport to disapprove the contract entered into between plaintiff and the Cities Service Gas Company under the terms of which plaintiff pays to said Cities Service Gas Company the price of 40 cents per M. c. f. for gas sold and delivered to it at the city gate for domestic purposes and in so far as they and each of them purport to disallow as an item of plaintiff's operating expense any sum paid for purchased gas in excess of 30 cents per M. c. f., are unlawful, unreasonable, arbitrary and void for the reasons set out in plaintiff's bill of complaint as follows:—

(a) For the reason that in said opinions, findings and orders said Commission found the value of the property or rate base of the Cities Service Gas Company to be $73,148,510; that the earnings of said company for the year ending June 30, 1932, were $7,963,813 applicable to replacement reserves and return on the fair value of the property; that replacement reserves for said period should be $1,977,591 and that the net income after reserves applicable to return on the value of said property was $5,986,222, which amounts to an earning of only 8.1837 per cent on said Com- [fol. 293] mission's own rate base so found and said Commission's own allowance for replacement reserves, and an earning of only 8.0438 per cent if the sum of $52,297.13 wrongfully and unlawfully disallowed by said Commission as an item of operating expense on account of it being paid to Henry L. Doherty & Company and if the item of $50,000 wrongfully and unlawfully disallowed by said Commission as an item of operating expense for the reason that it represented expenses incurred in said proceedings before said Commission be included in expenses. And plaintiff alleges that said earning is less than a reasonable rate of return for said Cities Service Gas Company considering the unusual hazards of its business and is less than a return necessary to attract capital to said business at this time and under present conditions, it therefore being apparent on the face of said opinions, findings and orders that the contract between plaintiff and the Cities Service Gas Company.

is reasonable, does not indicate any absence of arm's length dealing between plaintiff and said company on account of their affiliation and should not have been disapproved.

(b) For the reason that the attempt of said Commission in said opinions, findings and orders, and each of them, to avoid the clear and undisputed reasonableness of the earnings of the said Cities Service Gas Company by averaging the earnings over a period of years and applying same to an average value of property, is unreasonable, unjust and unlawful and does not change or alter the Commission's [fol. 294] findings that said Cities Service Gas Company earned only 8.1837 per cent on the value of its property found by said Commission after deducting reserves approved by said Commission, said Commission having no jurisdiction, power or authority to determine the present reasonableness or unreasonableness of said contract on the property values and earnings of said Cities Service Gas Company as of any time other than the time said opinions, findings and orders were entered.

(c) For the reason that said opinions, findings and orders on their face show the contract between plaintiff and the Cities Service Gas Company to be such a contract as would have been entered into by parties unaffiliated dealing at arm's length and in the general and open market subject to the usual safeguards of bargaining and competition.

(d) For the reason that said Commission in dealing with the item of interest during construction, as appears in Exhibit "C," pages 78 and 79, found that 6 per cent was a proper rate to use for this item notwithstanding the fact that it is common knowledge of which the Court may take judicial notice that money could not be procured at the time of said hearing at such rate and notwithstanding the fact that the Commission found 7 per cent to be a proper rate of return for the Cities Service Gas Company after the completion of its plant and after the same was placed in operation, said Commission by adopting said 6 per cent having thereby eliminated from the rate base of the Cities Service Gas Company approximately one million dollars.

(e) For the reason that in its consideration of the item of going value as appears in Exhibit "C," pages 85 to 88,

the Commission unlawfully, unreasonably, arbitrarily and capriciously allowed only the sum of $4,000,000 on its own valuation of $73,148,510 and ignored all the evidence in the case on the subject, such evidence consisting of the testimony of F. C. Hamilton, engineer for plaintiff, that a [fol. 296] proper allowance would be $8,808,582, and the testimony of its own witness, E. B. Black, that such value was $3,820,00 , and ignored the uniform practice of courts and commissions to allow for such item approximately 10 per cent of the rate base, by which arbitrary and unreasonable action said Commission reduced the proper rate base of said Cities Service Gas Company over six million dollars.

(f) For the reason that said Commission in its consideration of the item of gas leases and reserves of said Cities Service Gas Company after finding that the present fair market value of such reserves was $6,279,237 and the present book value $6,573,489.70, as appears in Exhibit "C" at pages 99 and 100, unreasonably and arbitrarily found that most of said reserves were not used and useful and allowed for said item only the sum of $2,874,990, thereby eliminating from the rate base of the Cities Service Gas Company the sum of $3,404,847, which on its own finding of present market value should have been included; and said Commission on rehearing wrongfully refused to permit plaintiff to show that the reserves allowed by said Commission were inadequate and would result in absolute failure of service as is shown by Exhibit "G" hereto attached. By all of which unreasonable, arbitrary and unwarranted conduct said Commission undertook, without one word of evidence from any witness in support of its finding as to what would constitute proper reserves for said Cities Service Gas Company, to substitute its own judgment and to usurp the duties of the officers of said company upon whom the responsibility for service rests.

(g) For the reason that said Commission eliminated from the replacement reserves of the Cities Service Gas Company all lease rentals and development expense on leases which it wrongfully found to be not used and useful, amounting to the sum of $532,530.77, as appears from said order, Exhibit "C," at page 112, and also eliminated the [fol. 296] reserve which must be accrued for amortizing the cost of said leases amounting to $514,981.68, as appears

from said order, Exhibit "C," page 112, or a total of $847,512.45.

(h) For the reason that said Commission in determining the rate base of the Cities Service Gas Company depreciated overheads, thereby eliminating from said rate base the sum of $1,014,392 without making any allowance in replacement reserves to compensate for such depreciation, which reserve should have been included in the amount of $30,443 annually, as appears by the opinion of said Commission, Exhibit "C," page 111, or said overheads should not have been depreciated and said rate base should have been accordingly increased.

(i) For the reason that it is apparent on the face of said opinions, findings and orders that if said Commission had made proper allowances in the rate base of the Cities Service Gas Company for interest during construction, going value and leases and gas reserves, and had made a reasonable allowance for replacement reserves, the rate base of said Cities Service Gas Company would be so increased and its earnings after replacement reserves so decreased on the Commission's own findings that the present earnings of said company after reserves and applicable for return would amount to less than 6½ per cent on such rate base.

(j) For the reason that said Cities Service Gas Company is engaged in inter-state commerce the right to control which is vested by the Constitution of the United States exclusively in Congress, and said Commission is without [fol. 297] jurisdiction to fix a rate for said Company or to proceed in the manner attempted in said proceedings so instituted by it or to make the orders herein set out.

(k) For the reason that the value of the property of the Cities Service Gas Company used and useful in carrying on its said business on August 31st, 1932, and at all times since that date, was and is not less than $105,857,402, and the finding by said Commission in said opinion and orders of August 31st, 1932, that said value was only the sum of $73,148,510 is unreasonable, unjust and contrary to all the evidence introduced before said Commission.

(l) For the reason that if the price of 30 cents for gas sold for domestic purposes at the city gate by the Cities Service Gas Company had been in effect during the year

ending June 30, 1932, and if said rate of 30 cents per M. c. f. is applied to the actual business transacted by said Cities Service Gas Company for said period, its gross earnings would have been reduced in the sum of $1,926,145.07 and its net earnings before replacement reserves would have been $5,935,371.78, which is a return of only 5.4 per cent on said Commission's own rate base as found in said opinion and orders of $73,148,510, which rate base is entirely unreasonable, unjust and inadequate as hereinbefore alleged after deducting the Commission's own unreasonable, unjust and inadequate allowance for replacement reserves, and if said rate had been so applied during said period the earnings of the Cities Service Gas Company would have amounted to only 5.6 per cent on the present fair value of its property of $105,857,402 for all the purposes of replacement reserves, depreciation, amortization, depletion and return.

[fol. 298] (m) For the reason that in its consideration of the reasonableness of said contract between plaintiff and Cities Service Gas Company for plaintiff's supply of gas at the city gate it was the duty of said Commission, in the absence of any jurisdiction, power or authority over the interstate business of said company to consider its operations, business and experience as the same actually existed and were being carried on by said company, without undertaking or attempting to determine the reasonableness or usefulness of its gas reserves or any other item of its property and without undertaking or attempting to determine the reasonableness of its operating expenses, or any item thereof, the jurisdiction of said Commission being limited to the determination of the reasonableness of such contract under existing operating conditions of the Cities Service Gas Company and said Commission being without jurisdiction, power or authority to regulate said company as attempted in said opinions, findings and orders.

(n) For the reason that said Commission has no jurisdiction, power or authority in a proceeding of the nature held by it and in the absence of any issue as to proper rates to be charged by this plaintiff to determine the moot question of the reasonableness of an item of plaintiff's operating expenses.

(o) For the reason that the finding of said Commission that the contract between plaintiff and Cities Service Gas Company was unreasonable and its order prohibiting plaintiff from setting up on its books any payments due under said contract and prohibiting plaintiff from taking such payments into consideration in fixing rates for its consumers is contrary to all evidence introduced before said Commission in said proceedings and is entirely without support in the evidence.

[fol. 299] (p) For the reason that the assumption of jurisdiction by said Commission in issuing the order for investigation, Exhibit "A", herein and all subsequent proceedings of said Commission under said order are in direct violation of Chapter 239 of the Session Laws of the State of Kansas of 1931 under which statute the right of the Commission to disapprove contracts and disallow items of operating expense is limited to proceedings, the purpose of which is to ascertain the reasonableness of a rate or charge to be made by a public utility.

Defendants answering further allege that the orders of said Commission in so far as they purport to disapprove the contract entered into between plaintiff and The Cities Service Gas Company and in so far as they disallow items of plaintiff's operating expense, any sum for purchase of gas in excess of 30 cents per M. c. f. are reasonable and valid.

26

Defendants deny the allegations in paragraph twenty six in plaintiff's bill of complaint in which plaintiff further alleges that said opinion and orders of said Commission entered August 31st, 1932, and each and all of them, in so far as they purport to find unreasonable the contract between the plaintiff and Henry L. Doherty & Company under which plaintiff pays to said Henry L. Doherty & Company $1\frac{3}{4}$ per cent of its gross revenues, are unreasonable, unjust and unlawful and void for the following reasons:

[fol. 300] (a) For the reason that said Commission has no jurisdiction, power or authority in a proceeding of the nature held by it and in the absence of any issue as to proper rates to be charged by this plaintiff to determine the moot question of the reasonableness of an item of plaintiff's operating expenses.

(b) For the reason that said Commission in said investigation so held by it did not have before it any evidence whatever as to the value of plaintiff's property used and useful in rendering the service in which it is engaged, its operating experience or the reasonableness of its existing rates, and unlawfully, unreasonably and unjustly refused to permit plaintiff to introduce any such evidence and was therefore not in a position to determine whether or not the disallowance of said item of operating expense would affect the rates then being charged by plaintiff or warrant a decrease in rates to consumers.

(c) For the reason that said Commission was without jurisdiction, power or authority to disallow said item of plaintiff's operating expense in the absence of an express finding that existing rates were unreasonable by reason of the inclusion of said item in plaintiff's operating expenses and the substitution of a new rate in lieu of the old rate so found to be unreasonable.

(d) For the reason that plaintiff offered to show to said Commission in said original proceeding and on rehearing, as shown by Exhibit "F" hereto attached, that under existing rates it was earning only 7.2 per cent on the present fair value of its property, and the disallowance of said item in plaintiff's operating expenses could not possibly affect the reasonableness of its existing rates or give jurisdiction to the Commission to reduce the same on account of the disallowance of said item.

[fol. 301] (e) For the reason that said Commission by disapproving and disallowing a contract entered into by the officers and directors of plaintiff in accordance with their business judgment has unlawfully and unreasonably undertaken the management of plaintiff's property and has undertaken to substitute its judgment for the judgment of the officers and directors of plaintiff in regard to a matter of business policy.

(f) For the reason that the finding of said Commission that the contract between plaintiff and Henry L. Doherty & Company was unreasonable and its order prohibiting plaintiff from setting up on its books any payments due under said contract and prohibiting plaintiff from taking such

payments into consideration in fixing rates for its consumers is contrary to all evidence introduced before said Commission in said proceeding and is entirely without support in the evidence, while in truth and fact services of great value were and are being rendered by said Henry L. Doherty & Company, to wit: the amount charged.

Defendants answering further allege that the opinion and orders of the Commission entered August 31, 1932, in so far as they purport to find unreasonable the contract between the plaintiff and Henry L. Doherty & Company under which the plaintiff pays to Henry L. Doherty & Company $1\frac{3}{4}$ per cent of its gross revenues, are reasonable and valid, and is a proper exercise of the jurisdiction, power and authority of the Public Service Commission for the State of Kansas.

27

Defendants deny all of the allegations of paragraph twenty-seven of plaintiff's bill of complaint except that [fol. 302] they admit that Exhibit "M" directing plaintiff to reduce its rates to consumers as of September 1, 1932, is in violation of the statutes of the State of Kansas.

28

Defendants deny the allegations of paragraph twenty-eight, set out in plaintiff's bill of complaint, and answering further allege that all the distributing companies joined in the investigation before the Commission were similarly situated and all of their interests were common in the matters under investigation by the Commission, and that plaintiff was lawfully compelled to appear before the Commission for the purpose of investigating the reasonableness of charges made by affiliated or holding companies.

The defendants answering further allege that all of the voting stock except qualifying directors' share, of the Cities Service Gas Company, plaintiff herein, is owned by the Empire Gas & Fuel Company, and that all of the voting stock, except qualifying directors' share, of the Empire Gas & Fuel Company, is owned by the Cities Service Company; that all of the voting stock, except qualifying directors' shares, of the plaintiff company is owned by the Gas Service Company; that all of the voting stock of the Gas Service Company is owned by the Cities Service Company; that

because of this ownership and control of the plaintiff company, and the Cities Service Gas Company by the Cities Service Company, they are subjected to one management and are not able to deal freely at arm's length with each other; that Henry L. Doherty & Company owns for all practical purposes the voting control of the common stock of the Cities Service Company and that under a contract between Henry L. Doherty & Company, plaintiff and the de-
[fol. 303] fendant distributing companies, and all other companies affiliated with the Cities Service Company, Henry L. Doherty & Company is for all practical purposes operator and manager of both the plaintiff and the Cities Service Gas Company, and that the Auditor of Henry L. Doherty & Company, who is appointed by Henry L. Doherty, is given the authority to appoint or remove any officer holding a responsible position in the plaintiff company, or the Cities Service Gas Company.

29

Defendants deny all the allegations set out in paragraph twenty-nine of plaintiff's bill of complaint.

30

Defendants have no information sufficient to enable them to affirm or deny the allegations that plaintiff cannot procure gas for less than 40 cents per M. c. f., but defendants are informed and believe and so aver that said plaintiff has made no reasonable or diligent effort to procure gas for less than 40 cents per M. c. f.

These answering defendants further say that both the plaintiff and the Cities Service Gas Company are thru stock ownership owned and controlled by the Cities Service Company and because of such relationship it is not in position to negotiate with the Cities Service Gas Company as to the price paid for gas, but it must pay and the Cities Service Gas Company must receive the price dictated by the Cities Service Company.

[fol. 304] 31

Defendants deny all of the allegations set out in paragraph thirty-one of the plaintiff's bill of complaint.

32

The defendants have no information sufficient to enable them to affirm or deny the allegations set out in paragraph thirty-two of the bill of complaint in which it is alleged that the State of Texas has placed an absolute and unqualified limit on the takes of wells in the gas reserves of the Cities Service Gas Company in Texas. Defendants answering further allege that if such an order were put into effect it would tend to decrease the value which the Commission placed upon the gas reserves and would not tend to limit the amount of gas which could be taken from such reserves, and that the gas reserves allowed by the Commission as set out in the plaintiff's bill of complaint are entirely adequate, sufficient, and reasonable.

33

Defendants deny that plaintiff is without adequate remedy at law and will suffer irreparable injury unless the injunctive relief prayed for is accorded. These defendants answering further allege that the order issued by the Commission on August 31, 1932, was the reasonable exercise of the jurisdiction conferred upon them by the laws of the State of Kansas, and that the plaintiff has not thereby been denied any of the rights which they may have under the constitution of the State of Kansas or the constitution of the United States.

[fol. 305] Defendants admit that that part of its order, Exhibit "M" to plaintiff's bill of complaint, dated August 31, 1932, wherein the defendant commission ordered the distributing companies from and after September 1, 1932, to deduct the excess between what the distributing companies were then paying for gas at the city gate and thirty cents per M. c. f. of gas and pass the difference to the consumer, is null and void, and further allege that these defendants have abandoned said order and allege that said Commission now has no intention of enforcing or attempting to enforce said order; that the defendant Commission relies upon and alleges it has the right to enforce its order made on August 31, 1932, Exhibit "L" attached to plaintiff's bill of complaint, whereby it ordered said distributing companies to show cause why they and each of them should not pass said reduction in price to be paid for gas at the city gate on to the consumers and in this connection these

defendants allege that such proceedings contemplate that an investigation be made as required by law as to each of said distributing companies to determine whether the earnings of said distributing company based upon the fair value of their property are excessive and unreasonable, after giving effect to the said thirty cent gate rate and all other facts bearing upon the question.

Defendants allege that unless and until said hearing is had and these defendants make an order determining that said rate to the consumers be reduced, that its said order, Exhibit "L," will not and may not affect the plaintiff, and that until an order is made reducing said rate to said distributing companies by the consideration of said reduced gate rate this court has not and will not have jurisdiction of the subject matter of this action.

[fol. 306] Wherefore Defendants, having answered all and singular those parts of the bill of complaint material and necessary to answer, pray that notwithstanding they have answered all the allegations of the bill of complaint that the court dismiss the bill of complaint for the reason and on the ground that it plainly appears from the averments therein contained that no federal question is raised by the bill of complaint and this court is without jurisdiction to try the cause. But these answering defendants reserve and save to themselves all of their rights in the presentation of evidence and request a hearing upon the matters of the issues of fact and law involved in this cause, in the event it should be determined that said bill of complaint be not dismissed for want of jurisdiction appearing therein; and further defendants pray plaintiff take nothing by reason of the allegations in said bill of complaint; that no permanent injunction be granted herein, but that these defendants be hence dismissed with reasonable costs and charges.

Chas. D. Welch, Harry Castor, Chas. W. Steiger,
E. H. Hatcher, Attorneys for Defendants.

[File endorsement omitted.]

[fol. 307] In United States District Court

Answer of Defendants in Case No. 1646 N Filed Oct. 3, 1932

The joint and several Answer of the Public Service Commission of the State of Kansas, J. W. Greenleaf, Thurman Hill and Charles W. Campbell, to the bill of complaint of the Cities Service Gas Company, a corporation, plaintiff.

These defendants now, and at all times hereafter, saving and reserving to themselves and each of them, all benefit and advantage of exception which can or may be had or taken to the many errors, uncertainties and other imperfections in the said bill of complaint contained, for answer thereunto or unto so much and such parts thereof as these defendants are advised is or are material or necessary for them to make answer unto, them, these defendants severally answering, say:

[fol. 308] I

They admit the allegations of paragraph one of said bill of complaint.

II

Defendants admit the allegations of paragraph two set out on page four of the bill of complaint, and deny all of the allegations of paragraph two set out on page five of the bill of complaint, and further deny and it is not true that the orders issued by the Commission, dated August 31, 1932, and attached to the bill of complaint as Exhibits "A" and "B" are confiscatory of plaintiff's property used and useful, in furnishing service and natural gas to the defendant distributing companies, and denies that the orders therefore are in contravention of any section of the constitution of the United States or any amendment thereto.

Defendants answering further allege that the Cities Service Gas Company, through common stock ownership is owned and controlled by the Cities Service Company, and that all of the distributing plants made defendants herein and against which the orders of the Commission were directed are also through stock ownership owned and controlled by the Cities Service Company, and that because of the affiliation of the plaintiff, the Cities Service Gas Com-

pany and of the defendants, the distributing plants named herein, and the unity of control thus engendered, the interstate carriage of the gas by the Cities Service Gas Company is combined with its local distribution in what is in practical effect one organization; that the opportunity exists for one member of the combination to charge the other an unreasonable rate for the gas furnished, and this is in fact done, and the unreasonable charge is made in part the basis of the retail rate.

[fol. 309] III

Defendants admit the allegations of paragraph three of the bill of complaint except that defendant alleges that only about 42,000 acres of the 1,225,000 acres of the gas leases owned by plaintiff, are drilled and producing gas and that approximately 1,000,000 acres of said gas leases are not available to plaintiff's pipe lines, that most of said 1,000,000 acres are what is known as "Wild Cat" leases and that the remainder of its leases outside those situated in the sweet proven area in the Amarillo field are located in the Hugoton field in Kansas and Oklahoma, and that said leases in the Hugoton field consisting of approximately 123,440 acres, although valuable for gas, are distant from the plaintiff's pipe line a distance of ninety miles, and except that defendant denies that all of said 1,225,000 acres of gas leases were acquired for the purpose of insuring a dependable supply of gas for its customers, and defendant alleges that all of the gas leases of plaintiff in excess of 71,276 acres were acquired and are held for speculative purposes.

Answering further defendants allege that in all cases where the plaintiffs, by means of its said pipe line system delivered gas in wholesale quantities to other purchasers not affiliated with the plaintiff's, that the plaintiff is selling its gas at much less than 40 cents per M. c. f., or has [fol. 310] a monopoly on the pipe line business, so that the independent companies are unable to otherwise obtain gas, and must pay to the plaintiff such unreasonable charge as it may exact.

IV

Defendants admit the first two sub-paragraphs of paragraph four of the bill of complaint, but deny the last subparagraph, and further deny that the rates or prices at

which plaintiff has been or is now supplying the defendant distributing companies with natural gas are reasonable and lawful, and further deny that the agreements were entered into after negotiations allowing for the protection of the defendant distributing companies. Defendants admit the allegations contained in paragraph four in so far as it sets out the price which the defendant is charging each of the defendant distributing companies for pipe line gas. The defendants answering further, allege that the agreement under which the plaintiff sells pipe line gas to the defendant distributing companies is a day to day agreement and does not bind the defendants for any length of time.

V

Defendants admit the allegations of the first four and last sub-paragraphs of paragraph five of the bill of complaint but denies the allegations of the fifth sub-paragraph of paragraph five, and further deny that the evidence and [fol. 311] exhibits introduced, and the investigation before the Commission disclosed that the contracts between the plaintiff and defendant distributing companies were reasonable, and such contract as would be entered into by persons dealing at arm's length; that the fair value of the property of plaintiff on September 1, 1931, used or useful, in the business of supplying natural gas to the defendant distributing companies, was $105,857,402.00, and alleges that the value of the plaintiff's property used or useful in the business of supplying natural gas to the defendant distributing companies is and was materially less than this amount, and that its net earnings from operations after depreciation was greatly in excess of a reasonable return. The defendants further deny that the rate of return which each of the defendant distributing companies was making at the time of the investigation was inadequate, unreasonable or confiscatory.

VI

Defendants admit the allegations of paragraph six of the bill of complaint.

VII

Defendants admit the allegations of paragraph seven of the bill of complaint.

VIII

Defendants admit the allegations of first four sub-paragraphs of paragraph eight of the bill of complaint. Defendants have no information sufficient to enable them to [fol. 312] affirm or deny the allegations set out in sub-paragraphs five and six of paragraph eight of the bill of complaint as to what showing the defendant distributing companies could have made under such allegations as to the plaintiff's gas reserve. The defendants deny that the Public Service Commission wrongfully denied to each of the defendant distributing companies the right to make proof on the rehearing of the offer set out in the bill of complaint as Exhibit "A", but that the Commission rightfully permitted only the proof of the earnings, expenses and net income of the plaintiff for the year ending June 30, 1932, as this was the only new matter presented in the application for rehearing.

IX

The Defendants admit the allegations of fact made in paragraph nine of plaintiff's bill of complaint. [fol. 313] Defendants deny that at no time has the defendant held itself out as public utility or common carrier of gas, and has at no time engaged in the business of common carrier, and denies that the entire properties of plaintiff have been devoted chiefly to a private enterprise. Answering further defendants allege that plaintiff is holding itself out as a public utility and common carrier of gas. Defendants admit that part of plaintiff's gas moves in interstate commerce, but denies, and it is not true that all of such gas so moves. Defendants deny the allegation that the pipe line company did not submit itself to the jurisdiction of the Commission, and allege that the officers and employes of the plaintiff pipe line company appeared before the Commission and presented the case for the plaintiff pipe line company, and has assumed the cost of the investigation, and has already set up such cost for amortization purposes as an expense of the plaintiff pipe line company.

The Defendants admit that the contracts for gas made by the plaintiff to the defendant distributing companies were in existence prior to the investigation by the Public

Service Commission, but deny that such charges and rates are fair and reasonable.

[fol. 314] The defendants deny all of the allegations of paragraph eleven of the bill of complaint, and answering further allege that the Public Service Commission properly found the value of plaintiff's property used or useful in its business was only $73,148,510, and that the plaintiff's net depreciation allowance should be $1,977,591, and that the Commission's findings that 30 cents per M. c. f. was a proper charge for the plaintiff to make to the defendant distributing companies, was reasonable and proper and within the jurisdiction of the Commission, due to the affiliated relationship between the plaintiff and the defendant distributing companies, and the orders were not in interference with inter-state commerce; nor impairment of the operation of contractual rights, nor in contravention to the constitution of the United States as amended.

XII

The Defendants deny the allegations of paragraph twelve of the bill of complaint, and further deny that 30 cents per M. c. f. for gas furnished will not afford the plaintiff a fair return upon the fair value of its property used and useful in its business, and deny that such return will be confisca-
[fol. 315] tory, or that plaintiff's property will be taken without due process of law, or the obligations of contract will be interfered with. The defendants answering further allege that the order of the Public Service Commission set out as Exhibits "H" and "I", in plaintiff's bill of complaint, are not addressed to the plaintiff, and do not in any way interfere with its property or contract right, and that it shows upon the face of the bill of complaint that the rights of the plaintiff are in no way interfered with.

XIII

Defendants deny all of the allegations of paragraph thirteen of the bill of complaint, and further deny the allegation that for the plaintiff to sell and deliver gas to the defendant distributing companies at the price fixed by the Public Service Commission in its orders would produce a fair and reasonable return on the value of its property used or useful in its business, and deny that the order would

result in the destruction of the plaintiff's property and business.

XIV

Defendants admit the allegations of fact in paragraph fourteen of the bill of complaint in so far as it alleges the [fol. 316] ownership of stock and corporate relationship of the Empire Gas and Fuel Company, and Cities Service Gas Company, the Cities Service Company, the Gas Service Company, and the defendant distributing companies, but denies that the plaintiff and defendant distributing companies are affiliated companies only because of technical provisions of Chapter 259 of the Session laws of the State of Kansas for 1931, and that the business of the plaintiff and the defendant distributing companies is carried on in an independent manner as if such affiliation did not exist, and denies that the common owner of both the plaintiff and defendant distributing companies would not be benefited from profits of the plaintiff, Cities Service Gas Company. The defendants answering further allege that all of the voting stock, except qualifying director's share, of the Cities Service Gas Company, plaintiff herein, is owned by the Empire Gas and Fuel Company, and that all of the voting stock except qualifying directors' share, of the empire Gas and Fuel Company, is owned by the Cities Service Company; that all of the voting stock, except qualifying directors' shares, of the defendant distributing companies, is owned by the Gas Service Company, and that all of the voting stock of the Gas Service Company is owned by the Cities Service Company; that because of this ownership and control of the plaintiff company, and the defendant distributing companies by the Cities Service Company, they are subjected to one management and are not able to deal freely at arm's length with each other; that Henry L. Doherty & Company owns for all practicable purposes the [fol. 317] voting control of the common stock of the Cities Service Company, and that under a contract between Henry L. Doherty & Company, plaintiff and the defendant distributing companies, and all other companies affiliated with the Cities Service Company, Henry L. Doherty & Company is for all practical purposes operator and manager of both the plaintiff and defendant distributing companies, and that the Auditor of Henry L. Doherty & Company who is

appointed by Henry L. Doherty, is given the authority to appoint or remove an officer holding a responsible position in the plaintiff company, or the defendant distributing companies.

XV

Defendants deny all of the allegations of paragraph fifteen of the plaintiff's bill of complaint, and further deny that the Public Service Commission arbitrarily and capriciously substituted its judgment for the judgment of the officers and directors of the plaintiff in finding the amount of gas reserve necessary to adequately supply plaintiff's customers, and wrongfully excluded from the valuation of plaintiff's property all other gas lines owned by it. The defendants answering further allege that the Public Service Commission included in the valuation of plaintiff's property [fol. 318] gas reserves in an amount sufficient to last it over a period of twenty years, and that such allowance was liberal to the extent of unreasonableness, and was a greater allowance than the present customers of the plaintiff company should be required to carry. Defendants further allege that a great number of the gas reserves that the respondents contended should be placed in the valuation of the plaintiff's property are of doubtful value for gas and were from fifty to ninety miles from the plaintiff's pipe line, and could not be used, and is not used and useful in the plaintiff's business of supplying natural gas to the defendant distributing companies, and that the same were acquired and held for speculative purposes.

XVI

The defendants admit all of the allegations of fact in paragraph sixteen of the plaintiff's bill of complaint, except the allegations and conclusions pertaining to the Public Utility laws of the State of Kansas, and to the statements relating thereto set out in the last part of said paragraph.

[fol. 319]

XVII

Defendants admit all of the allegations of fact contained in paragraph seventeen of the bill of complaint, except the last sentence, which defendants deny, and further deny that the price which the plaintiff company charges the defendant distributing companies for gas is a fair and reason-

able price, and answering further the defendants allege that the price charged by the plaintiff to the defendant distributing companies for gas is unfair and unreasonable and is in excess of the amount necessary for the plaintiff to receive in order to maintain its said pipe line system and business and produce a reasonable profit therefrom.

XVIII

Defendants deny all the allegations in paragraph eighteen of plaintiff's bill of complaint and defendants answering further allege that Henry L. Doherty & Company has in addition to the 1¾ per cent of the annual gross income from sale of natural gas to persons and companies other than the distributing companies, defendants herein, and other affiliated companies, charged the plaintiff company specifically for all services rendered and that the 1¾ per cent payment has gone into the treasury of the Cities Service Company to take care of its operating expenses and the cost of selling its securities and the plaintiff and the defendant distributing companies have derived no benefit [fol. 320] therefrom; answering further paragraph eighteen of plaintiff's bill of complaint, defendants allege that a reduction of ten per cent in the price of gas sold to the defendant distributing companies by the plaintiff would net the plaintiff company a reasonable return upon the value of its property used and useful in serving its customers.

XIX

Defendants deny all the allegations in paragraph nineteen of plaintiff's bill of complaint; answering further defendants allege that the Commission proceeded under the investigation of the reasonableness of charges made by holding or affiliated companies to the defendant distributing companies in an orderly manner and under the jurisdiction vested in them by the statutes of Kansas, and after a careful investigation in which it considered all of the evidence it found that 30 cents per M. c. f. was a reasonable price for the plaintiff to charge to the affiliated distributing companies for gas, and issued an order in accordance therewith, being Exhibit "H" of plaintiff's bill of complaint, and in conformity with the laws of the State of Kansas regu-

lating the practices and acts of public utilities, and such order is reasonable and lawful.

[fol. 321] XX

Defendants deny all the allegations of paragraph twenty in plaintiff's bill of complaint, and answering further allege that the Commission took into consideration the plaintiff's system as a whole in arriving at the value of its property used and useful in serving its consumers and arrived at a uniform rate for the system as a whole in conformity with the evidence submitted in the investigation and the allegations of respondents that the plaintiff system was not possible of segregation into zones for the purpose of fixing rates and by this process the Commission considered all the property of the plaintiff and made a liberal allowance for gas reserves for the future use of plaintiff in serving its customers, and the proceedings and findings of the Commission are reasonable and should be permitted to stand.

XXI

The defendants deny all the allegations of paragraph twenty one in plaintiff's bill of complaint and allege further that the order of the Commission finding .30 cents per M. c. f. to be a reasonable price for gas sold by the plaintiff to the defendant distributing companies is reasonable and will cause no loss in the assets and properties of the plaintiff company.

[fol. 322] XXII

Defendants admit that each and all the distributing company defendants are interested in the subject matter of this controversy and allege further that each and all distributing company defendants have filed separate and several complaints in the subject matter of this controversy, but defendants deny that the distributing company defendants will be compelled to breach their respective gas purchase contracts with the plaintiff if the orders of the Commission are permitted to stand, and further allege that if a reasonable price is charged by the plaintiff herein to the distributing company defendants for gas as found by the Commission, and under the law required, the contract rights of the plaintiff will not be affected.

XXIII

The defendants deny that the orders complained of herein violate any of the plaintiff's rights under the federal constitution and deny that the orders in any way interfere with inter state commerce.

XXIV

Defendants deny all the allegations of paragraph twenty four of the bill of complaint.

[fol. 323] XXV

Defendants deny all the allegations of paragraph twenty five of the bill of complaint and allege that if the plaintiff will charge a reasonable price for gas sold to the distributing company defendants as found by the Commission and required by law, its business will not be interfered with

XXVI

Defendants further answering deny that the plaintiff has no plain, speedy or adequate remedy at law. Defendants admit that that part of its order, Exhibit "I" to plaintiff's bill of complaint, dated August 31, 1932, wherein the defendant commission ordered the distributing companies from and after September 1, 1932, to deduct the excess between what the distributing companies were then paying for gas at the city gate and thirty cents per M. c. f. of gas and pass the difference to the consumer, is null and void, and further allege that these defendants have abandoned said order and allege that said Commission now has no intention of enforcing or attempting to enforce said order; that the defendant Commission relies upon and alleges it has the [fol. 324] right to enforce its order made on August 31, 1932, Exhibit "H" attached to plaintiff's bill of complaint, whereby it ordered said distributing companies to show cause why they and each of them should not pass said reduction in price to be paid for gas at the city gate on to the consumers and in this connection these defendants allege that such proceedings contemplate that an investigation be made as required by law as to each of said distributing companies to determine whether the earnings of said distributing company based upon the fair value of their property are excessive and unreasonable, after giving effect to the said

thirty cent gate rate and all other facts bearing upon the question.

Defendants allege that unless and until said hearing is had and these defendants make an order determining that said rate to the consumers be reduced, that its said order, Exhibit "H", will not and may not affect the plaintiff, and that until an order is made reducing said rate to said distributing companies by the consideration of said reduced gate rate this court has not and will not have jurisdiction of the subject matter of this action.

Wherefore Defendants have answered all and singular those parts of the bill of complaint material and necessary to answer, pray that notwithstanding they have answered all the allegations of the bill of complaint that the [fol. 325] court dismiss the bill of complaint *that the court dismiss the bill of complaint* for the reason and on the ground that it plainly appears in the averments therein contained that the plaintiff has failed to state a cause of action over which this court has jurisdiction. But these answering defendants save and reserve to themselves all their rights in the presentation of evidence and request a hearing upon the matters of the issues of fact and law involved in this cause in the event it should be determined that said bill of complaint be not dismissed for the want of jurisdiction of this court; and further defendants pray that plaintiff take nothing by reason of the allegations in this said bill of complaint; that no permanent injunction be granted herein, but that these defendants be hence dismissed with reasonable costs and charges.

Chas. D. Welch, Harry Castor, Chas. W. Steiger, E. H. Hatcher.

[File endorsement omitted.]

[Fol. 320] In United States District Court for the District of Kansas, First Division

In Equity. No. 1637 N

The Wichita Gas Company, a Corporation, Plaintiff,

vs.

The Public Service Commission of the State of Kansas et al., Defendants

In Equity. No. 1638 N

The Hutchinson Gas Company, a Corporation, Plaintiff,

vs.

The Public Service Commission of the State of Kansas, et al., Defendants

In Equity. No. 1639 N

The Newton Gas Company, a Corporation, Plaintiff,

vs.

The Public Service Commission of the State of Kansas, et al., Defendants

In Equity. No. 1640 N

The Pittsburg Gas Company, a Corporation, Plaintiff,

vs.

The Public Service Commission of the State of Kansas, et al., Defendants

In Equity. No. 1641 N

The Capital Gas & Electric Company, a Corporation, Plaintiff,

vs.

The Public Service Commission of the State of Kansas, et al., Defendants

In Equity. No. 1642 N

THE WYANDOTTE COUNTY GAS COMPANY, a Corporation, Plaintiff

vs.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, et al., Defendants

In Equity. No. 1643 N

[fol. 327] THE GIRARD GAS COMPANY, a Corporation, Plaintiff,

vs.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, et al., Defendants

In Equity. No. 1644 N

UNION PUBLIC SERVICE COMPANY, a Corporation, Plaintiff,

vs.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, et al., Defendants

In Equity. No. 1645 N

THE WESTERN DISTRIBUTING COMPANY, a Corporation, Plaintiff,

vs.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, et al., Defendants

In Equity. No. 1646 N

CITIES SERVICE GAS COMPANY, Plaintiff,

vs.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, et al., Defendants

Appearances:

For Plaintiffs: James W. Finley, R. E. Cullison, Chas. A. Frueauff, Robt. S. Sloan, Fred Robertson, J. O. Emerson, Robt. D. Garver, Robert Stone.

For Defendants: Chas. D. Welch, Harry Castor, Chas. W. Steiger, E. H. Hatcher.

Before Phillips and McDermott, Circuit Judges, and Hopkins, District Judge.

OPINION Filed Jan. 5, 1933

PHILLIPS, circuit judge, delivered the opinion of the court:

The Cities Service Gas Company, a Delaware corporation, is engaged in the business of producing and transporting gas from Texas and Oklahoma and delivering it to distributing companies along its line, among which are the [fol. 328] following in the state of Kansas: The Wichita Gas Company, The Hutchinson Gas Company, The Pittsburg Gas Company, The Capital Gas & Electric Company, The Newton Gas Company, The Girard Gas Company, The Wyandotte County Gas Company, The Union Public Service Company, and The Western Distributing Company.

The common stock of each of such distributing companies, except the qualifying directors' shares, is owned by the Gas Service Company, a corporation. The stock of the Gas Service Company, except the qualifying directors' shares is owned by the Cities Service Company, a Delaware corporation. The stock of the Cities Service Gas Company, except the qualifying directors' shares, is owned by the Empire Gas & Fuel Company. The stock of the Empire Gas & Fuel Company, except the qualifying directors' shares, is owned by the Cities Service Company.

The Western Distributing Company is a West Virginia corporation and a citizen of that state. The Union Public Service Company is a Delaware corporation and a citizen of that state. The other distributing companies are Kansas corporations.

The Cities Service Gas Company furnishes gas to the distributing companies at the city gates under day to day contracts, which are oral, at forty cents per thousand cubic feet. Each of the distributing companies has contracted to pay Henry L. Doherty & Company one and three-fourths per cent of the gross revenue, a per diem charge and expenses for certain specific services, and an engineering fee of five per cent of the cost of new construction, in consideration of which Henry L. Doherty & Company main-

tains legal, managerial, engineering, accounting and purchasing staffs whose services are available to the distributing companies.

Each of the distributing companies has also entered into a contract with the Gas Service Company under which the [fol. 329] latter furnishes and the former pays for certain services. This contract has been approved by the Commission and is not in controversy here.

On July 2, 1931, the Public Service Commission commenced a proceeding against the corporations hereinbefore named, except the Cities Service Company and the Cities Service Gas Company. It found that the reasonableness of the contracts hereinbefore referred to, and the charges made for services and commodities furnished thereunder, should be inquired into and a determination made of the amounts which properly should be set up as operating expense of the distributing companies on account of expenditures made for such commodities and services under such contracts, and entered an order on such findings for a hearing to inquire into the reasonableness of such contracts and charges, and directed that respondents in such proceeding furnish such information concerning such contracts as the Commission might desire, and "show cause why such holding company contracts, or service or commodity charges, should they be found to be unreasonable, should not be disallowed as operating expense of the distributing companies, and adjustment made in this respect as to charges made to the consumers."

After a hearing, the Commission on July 20, 1932, made findings to the effect that any amounts paid by the distributing companies under their contracts with Henry L. Doherty & Company were unreasonable, and that any amounts paid by the distributing companies to the Cities Service Gas Company for gas in excess of 29.5 cents per thousand cubic feet at the city gates were unreasonable, and ordered that on and after August 1, 1932, the distributing companies (1) cease setting up on their books as operating expenses the one and three-fourths per cent payments to Henry L. Doherty & Company and any payments for gas to the Cities Service Gas Company in excess of 29.5 cents per thousand cubic feet, (2) give no consideration to any such payments in fixing their rates to domestic [fol. 330] consumers, (3) reduce their rates to their con-

sumers proportionately, pending a final determination of their rates; and show cause on September 1, 1932, why such reductions should not be made permanent.

A petition for rehearing was filed by the respondents setting up fifty one grounds. A rehearing, limited to one of such grounds, was granted. After such rehearing, the Commission increased its finding of a reasonable charge for gas at the city gates from 29.5 to 30 cents, and with that modification and the necessary changes in dates, on August 31, 1932, re-entered its order of July 20 in the form of two orders.

The material portions of the first of such orders is as follows:

"That on and after the first day of September, 1932, the distributing companies, respondents above named, shall cease to set up on their books as an expense item any payments made to Henry L. Doherty & Company under the contract above mentioned, because of the one and three fourths per cent charge, and also any payments made to Cities Service Gas Company for main line town border gas in excess of 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

"That on the 17th day of October, 1932, the distributing companies, respondents above named, appear before the Public Service Commission, at 10 o'clock a. m., and show cause to the Commission why the reduction in expenses as above set forth should not be passed on to the consumers with such other reductions as may be found reasonable."

The material portions of the second of such orders is as follows:

"It is therefore by the Commission ordered, that effective September 1, 1932, and until a hearing is held and an order issued, that the distributing companies, respondents above named, shall charge rates to the consumers as follows:

"All distributing companies paying a gate rate in excess of 30 cents per M. C. F., shall deduct the difference between what the distributing company is now paying at the city gate and 30 cents per M. C. F. and pass on this difference to the consumer."

[fol. 331] The nine distributing companies and the Cities Service Gas Company brought separate suits in equity to enjoin the enforcement of the two orders of August 31, 1932.

The Newton Gas Company filed a cross bill in each of the suits brought by the distributing companies in which it challenged the right of the Commission to join it with the other utilities in one joint proceeding. Counsel for the Newton Gas Company have advised the court that they do not desire to press these cross bills.

These actions were commenced on September 19, 1932, within the thirty day period required by section 66 118, Revised Statutes of Kansas 1923.

The several bills alleged diversity of citizenship as to the Cities Service Gas Company, The Western Distributing Company and The Union Public Service Company, and alleged that the orders are confiscatory of plaintiff's property, impair the obligations of their contracts, deny to them the equal protection of the laws, and unconstitutionally interfere with interstate commerce. The bills of the distributing companies also alleged that the governor had directed the attorney general to bring suits to have them placed in the hands of receivers for the purpose of avoiding a judicial review of the orders of August 31, 1932.

An application was made for a temporary injunction. At the hearing thereon, the Commission confessed that the second order made on August 31, 1932, was in conflict with section 66 118, Revised Statutes of Kansas 1923, which prescribes that an order cannot become effective until thirty days after it is entered; and consented that the enforcement of such second order might be permanently enjoined. We granted a temporary injunction against the enforcement of both orders.

The cases were consolidated for trial. Upon the trial the evidence introduced before the Commission was received in [fol. 332] evidence, supplemented by an agreed abstract of such evidence, and by stipulations and other evidence.

Council for the Commission contend that the first order is not subject to any of the constitutional objections urged by the plaintiffs, namely, that it confiscates their property, interferes with their right to contract, and interferes with interstate commerce, because all that it does is to find that the contracts under inquiry are unreasonable,

and the extent of such unreasonableness. They urge that the order does not take any property from the Cities Service Gas Company, that it still may continue to collect the forty cent gate rate, that it does not take any property from the distributing companies, that they may still continue to charge their present rates until a valid order is made requiring them to make a decrease in their charges to their consumers, that it does not require the distributing companies to discontinue the contracts nor to discontinue any payments thereunder, and that such contracts remain in full force and effect.

There are two answers to this contention. The first order, entered August 31, 1932, expressly prohibits the distributing companies from giving consideration to the payments made to Henry L. Doherty & Company and to the Cities Service Gas Company for gas at the city gates in excess of thirty cents per thousand cubic feet "in fixing a rate for the domestic consumer" on and after September 1, 1932. These are two of the important items which enter into the cost upon which the distributing companies' rates are predicated, and the elimination thereof on September 1, 1932, from the rates charged the domestic consumers would have necessarily effected a substantial reduction in rates. Hence, the order is in substance and effect a rate reducing order.

But, if it is only an order adjudging the contracts unreasonable and determining the proper amount which may be [fol. 333] set up for expenditures thereunder as proper operating expense in determining rates for local consumers, and is only a preliminary step in a rate determination, the order is subject to review. Had the distributing companies failed to appeal from such order or seek a judicial review thereof within thirty days from August 1, 1932, it would have become final on September 1, 1932 (sec. 66-118, R. S. Kan. 1923), and the facts therein found would have become res adjudicata, and, in that event, at the hearing under the last paragraph of the second order, the companies could not have defended against an elimination of such items as a part of their operating cost in fixing their rates.

If the construction of counsel for the Commission is correct, the order is plainly an attempt to avoid a judicial review in this court of the matters therein determined, and to

deprive the distributing companies of their constitutional rights. This cannot be tolerated.

The power of a public service commission to inquire into contracts between the company furnishing the service or commodity, the rates for which are under inquiry, and its parent or holding company, has been the subject of judicial inquiry in recent cases. (See Note 1.)

[fol. 334] We think there can be no doubt, under the decision in Smith v. Illinois Bell Tel. Co., supra, and Western Distributing Co. v. Public Service Commission, supra, that the commission has power to inquire into the reasonableness of such contracts. The extent of such inquiry, however, has not been settled.

Counsel for plaintiffs contend that, while the Commis-

[fol. 335] sion may determine whether the contracts are fair and reasonable, and such as ordinarily prudent business men, dealing at arm's length, free from domination

Note 1

In Southwestern Bell Tele. Co. v. Public Service Commission, 262 U. S. 276, the court said:

"The commission is not the financial manager of the corporation and it is not empowered to substitute its judgment for that of the directors of the corporation; nor can it ignore items charged by the utility as operating expenses unless there is an abuse of discretion in that regard by the corporate officers."

Again, in United Fuel Gas Co. v. Railroad Commission of Kentucky, 278 U. S. 300, the court said:

"We recognize that a public service commission, under the guise of establishing a fair rate, may not usurp the functions of the company's directors and in every case substitute its judgment for theirs as to the propriety of con-

benefits from the contract and probably could not have secured better terms elsewhere."

But in Smith v. Illinois Bell Telephone Co., 282 U. S. 133, the court said:

"The Western Electric Company not only manufactured apparatus for the licensees of the Bell System, but engaged

of a parent corporation, under the existing facts and circumstances would enter into, or whether they exact an unfair and unconscionable charge for a commodity or service, it may not determine and fix the interstate rate charged for such commodity or service.

It has been settled by repeated decisions of the supreme court that a state commission has no power to fix and regulate contracts entered into by the utility; and common ownership is not of itself sufficient ground for disregarding such intercorporate agreements when it appears that, although an affiliated corporation may be receiving the larger share of the profits, the regulated company is still receiving substantial state interstate gas rates. Hence, a state commission cannot fix the price to be charged for natural gas transported from one state to another and sold and delivered in bulk to an independent distributing company. (Missouri, ex rel., Barrett v. Kansas Gas Co., 265 U. S. 298; Peoples Natural Gas Co. v. Public Service Comm., 270 U. S. 550; Public Utilities Comm. v. Attleboro S. & E. Co., 273 U. S. 83; Pennsylvania Gas Co. v. Public Service Comm., 252 U. S. 23; Public Utilities Co. v. Landon, 249 U. S. 236.)

On the other hand, a state does have the power to regulate the price of gas brought into a state and sold directly to the consumer, because "the business of supplying, on demand, local consumers is a local business, even though the gas be brought from another state and drawn for dis-

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in other large operations, and it cannot be merely assumed or conjectured that the net earnings on the entire business represent the net earnings from the sale to the Bell licensees generally or from those to the Illinois company. Nor is the argument of the appellants answered by a mere comparison of the prices charged by the Western Electric Company to the Illinois Company with the higher prices charged by other manufacturers for comparable material, or by the Western Electric Company to independent telephone companies. The point of the appellants' contention is that the Western Electric Company, through the organization and control of the American Company, occupied a special position with particular advantages in relation to the manufacture and sale of equipment to the licensees of the Bell System, including the Illinois Company, that is, that it was virtually the manufacturing department for

tribution directly from interstate mains; and this is so whether the local distribution be made by the transporting company or by independent distributing companies." (Missouri v. Kansas Gas Co., 265 U. S. 298, 309; Penna. Gas Co. v. Public Service Comm., 252 U. S. 23; East Ohio Gas Co. v. Tax Commission, 283 U. S. 465.)

We are of the opinion that the facts here justify the conclusion that the Cities Service Company, together with the Gas Service Company, the distributing companies, the Empire Gas & Fuel Company and the Cities Service Gas Com- [fol. 336] pany are engaged in a common enterprise, namely, the transporting and furnishing of gas to local consumers; that the Cities Service Company exercises such complete dominion and control over the Cities Service Gas Company and the distributing companies that, under the general rules of agency, the Cities Service Gas Company and the distributing companies are mere agencies or instrumentalities of the Cities Service Company; and that, in substance and effect, the Cities Service Company is, through such agencies, supplying gas to local consumers on demand and is engaged in a local business. If this be true, the Commission had the power to determine the rea-

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that system, and the question is as to the net earnings of the Western Electric Company realized in that department and the extent to which, if at all, such profit figures in the estimates upon which the charge of confiscation is predicated. We think there should be findings upon this point."

Again, in the recent case of Western Distributing Company v. Public Service Commission of Kansas, 285 U. S. 119, the court said:

"The appellant adverts to the fact that in its bill of complaint are included a number of averments not denied by the appellees. In brief these are that the company does be obtained from any other source; that the same rate is being charged to other distributing companies along the lines of the Cities Service Gas Company, and was being charged by another independent pipe line to another city; that an ineffectual effort had been made to find local gas available to El Dorado; and that appellant had attempted to get a lower rate from Cities Service Gas Company, but could not do so. It is urged that as these averments were

sonableness of the charge set up as operating expense for gas at the city gates in fixing the local rate. That could only be done by determining a reasonable return to the Cities Service Gas Company for producing, transporting and delivering such gas at the city gates.

However, if we grant that the Commission can only scrutinize and inquire into the reasonableness of such contracts, we are of the opinion that the same result necessarily fol not own or produce any natural gas; that the only source of supply for the city of El Dorado is the main of the Cities Service Gas Company; that no supply at a lower price can lows. Since the Cities Service Company enjoys a monopoly and affords the only reliable source for supplying gas to the distributing companies, the only method of determining the fairness and reasonableness of the charge at the city gates is to determine the reasonableness of the return to the Cities Service Gas Company on their property used and useful in the business. Any charge in excess of that for gas at the city gates, under the contract between two subsidiary corporations who have the same parent or holding corporation, would be unfair and unreasonable.

It follows that we must determine the value of the property of the Cities Service Gas Company used and useful in

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uncontradicted they constitute, when taken with the facts previously stated, a prima facie case for the reasonableness of the rate charged. This might well be true were it not for the fact of unity of ownership and control of the pipe line and the distribution system. An averment of negotiation and effort to procure a reduction in the wholesale rate means little in the light of the fact that the negotiators are both acting in the same interest—that of the holding company which controls both. All of these facts so averred in the pleadings would be far more persuasive with respect to the propriety of the rate if the parties were independent of each other and dealing at arm's length. Where, however, they constitute but a single interest and involve the embarkation of the total capital in what is in effect one enterprise, the elements of double profit and of the reasonableness of inter-company charges must necessarily be the subject of inquiry and scrutiny before the question as to the lawfulness of the retail rate based thereon can be satisfactorily answered."

the business of producing, transporting, and delivering gas, the amount of its earnings, and a fair return on such property. The case has been tried so that the facts necessary to make these determinations are before us.

[fol. 337] We have made and filed findings of fact and in the footnotes thereto expressed our reasons therefor, and in this opinion will only state the ultimate facts so found.

In determining these facts, we have kept in mind that the findings of the Commission are presumed to be correct. (Blanton v. Belt Line Ry. Corp., 268 U. S. 413, 422; Cotting v. Kansas City Stockyards Co., 183 U. S. 79; Denver Union Stockyard Co. v. United States [D. C. Colo.] 57 Fed. 2d 735, 739), but that, on the question of confiscation, the plaintiffs are entitled to the independent judgment of a judicial tribunal as to the law and facts. (United Railways & E. Co. v. West, 280 U. S. 234, 251; Bluefield W. W. & Imp. Co. v. Public Service Commission, 262 U. S. 679, 689; Ohio Valley W. Co. v. Ben Avon Borough, 253 U. S. 287; Lincoln Gas Co. v. Lincoln, 223 U. S. 349; Crowell v. Benson, 285 U. S. 22, 60.)

In the case last cited, the court said:

"In cases brought to enforce constitutional rights, the judicial power of the United States necessarily extends to the independent determination of all questions, both of fact and law, necessary to the performance of that supreme function. The case of confiscation is illustrative, the ultimate conclusion almost invariably depending upon the decision of questions of fact. This court has held the owner to be entitled to 'a fair opportunity for submitting that issue to a judicial tribunal for determination upon its own independent judgment as to both the law and facts.'"

The value of the property of the Cities Service Gas Company used and useful in its business of producing, transporting and supplying gas to the distributing companies at the city gates, was found by the Commission to be $73,170,510. We find such value to be at least $82,380,582. The net available annual return from such property was found by the Commission to be $7,161,793. We find such return to be $5,860,327, or a return of 7.11 per cent on the present value of the property.

If the charge made by the Cities Service Gas Company [fol. 338] for gas at the city gates was reduced to thirty

cents per thousand cubic feet, it would result in a reduction of $1,926,145.07 in its net income. This would reduce its return to 4.8 per cent on the present value of its property used and useful in the business.

We are of the opinion that a return of approximately eight per cent upon present values is necessary under present conditions to assure confidence in the financial soundness of the Cities Service Gas Company, to maintain its credit, and to enable it to raise money necessary for the discharge of its public duties, and that any return substantially lower than eight per cent would be confiscatory. (United Railways & E. Co. v. West, 280 U. S. 234, 252; Smith v. Bell Telephone Co., 282 U. S. 133, 161.)

The undisputed evidence shows that if the distributing companies are compelled to pay forty cents per thousand cubic feet for gas at the city gates and to base their rates to consumers on the price fixed as reasonable by the Commission in its order of August 31, 1932, they will have no earnings in excess of operating expenses to cover depreciation and afford any return on the value of their property used and useful in the business. Upon the trial, it was stipulated that the Cities Service Gas Company could not continue its business without the patronage of the distributing companies.

We conclude, therefore, that forty cents per thousand cubic feet for gas at the city gates is a reasonable charge; that to compel the Cities Service Gas Company to furnish such gas at thirty cents per thousand cubic feet will result in confiscation of its property, and that to compel the distributing companies to pay forty cents per thousand cubic feet for gas at the city gates and permit them to set up only thirty cents thereof in their operating expense, in fixing their rates to local consumers, will result in confiscation of the properties of the distributing companies.

[fol. 339] We have found that the distributing companies in their proof before the Commission failed to establish that the payments of one and three-fourths per cent under the Henry L. Doherty & Company contracts were fair and reasonable, and therefore proper items of expense to be considered in determining local rates for gas.

We set out the applicable provisions of the Kansas statute in Note 2.

Henry L. Doherty, doing business under the name of Henry L. Doherty & Company, has built up and maintains a complete organization for the designing, construction, operation, development, and management of public utilities, oil and natural-gas properties. This organization consists of 1,687 employees, among whom are included experienced executives, financial advisers, construction, valuation, electrical and oil and gas engineers, geologists, technicians, rate experts, accountants and operators. Henry L. Doherty & Company also maintains a department for the purchase, sale, promotion and transfer of stocks of the various subsidiary corporations of the Cities Service Company, a foreign oil department, a steamship and tank-car department, an oil-producing and refining department, and a real-estate division chiefly concerned with New York real estate.

As stated in our findings, the activities of Henry L. Doherty & Company embrace many matters not covered by [fol. 340] such contracts, the expense of which cannot properly be charged to the distributing companies.

The evidence before the Commission consisted of proof that Henry L. Doherty & Company is not operated for

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Note 2

Section 74-602c, 1931 Supp., R. S. Kan. 1923, is as follows:

"Showing required for fixing or charging rates. In ascertaining the reasonableness of a rate or charge to be made by a public utility, no charge for services rendered by a holding or affiliated company, or charge for material or commodity furnished or purchased from a holding or affiliated company, shall be given consideration in determining a reasonable rate or charge unless there be a showing made by the utility affected by the rate or charge as to the actual cost to the holding or affiliated company furnishing such service and material or commodity. Such showing shall consist of an itemized statement furnished by the utility setting out in detail the various items, cost for services rendered and material or commodity furnished by the holding or affiliated company."

profit, of the services rendered to the distributing companies by it, and of the cost and expense of maintaining The Henry L. Doherty & Company organization. There was no separate proof of the expense which might properly be allocated to the services rendered under such contracts. Therefore, we have concluded that the distributing companies failed to meet the requirements of the Kansas statute by showing in detail the items of service rendered under such contracts and the cost thereof. Furthermore, it was impossible to determine from the evidence before the Commission whether the charge for the services rendered by the distributing companies was fair and reasonable, because the proof was of the total cost and expense of maintaining Henry L. Doherty & Company, which included many activities unrelated to and of no benefit to the distributing companies; and there was no proper allocation of the cost and expense of such unrelated activities.

We are of the opinion that the burden of proof, both under the Kansas statute and under general principles, was upon the distributing companies (Smith v. Illinois Bell Tel. Co., supra, Michigan Law Review, Nov. 1932, pp. 16-24).

Counsel for the Commission contend that the services rendered by Henry L. Doherty & Company are a duplication of the services rendered by the Gas Service Company, and are therefore not necessary or useful to the distributing companies. With this we cannot agree. The Gas Service Company is equipped to render such services only in minor and relatively unimportant matters.

The expense of each distributing company maintaining a separate organization like that of Henry L. Doherty & [fol. 341] Company would be prohibitive. For that reason it is in keeping with sound business principles for it to contract with Henry L. Doherty & Company, or some similar organization, for such services. We therefore conclude that, while the services contracted for are necessary and useful to the distributing companies and that the contracts in that respect are proper, the proof adduced was insufficient to meet the requirements of the Kansas statute or to enable the Commission to determine whether the charges for such services were fair and reasonable.

Certain incidental matters require a limited discussion.

The Commission held that certain gas leases claimed to be held by the Cities Service Gas Company for gas reserves

were in excess of the required reserves, and that they were in fact being held for speculative purposes. The evidence established, and we have found, that the officers and directors of the Cities Service Gas Company, who are men of broad experience in the natural-gas business, in the exercise of an honest and, we think, sound business judgment, determined that such leases were necessary to afford it an adequate gas reserve, and that such leases were acquired and are held by it as bona fide reserves, and not for speculation.

The Commission was not empowered to substitute its judgment for that of the officers and directors of the Cities Service Gas Company as to the amount of leases necessary to afford an adequate gas reserve, in the absence of a showing of abuse of discretion by such officers in that regard. (Southwestern Bell Tel. Co. v. Public Service Com., 262 U. S. 276, 289; State Public Utilities Com. v. Springfield Gas & Elec. Co., 291 Ill. 209, 234, 125 N. E. 891; People v. Stevens, 203 N. Y. 7, 96 N. E. 114, 117; Idaho Power Co. v. Thompson [D. C. Ida.], 19 F. 2d 547, 580; Kansas City K. V. & W. Ry. Co. v. Bristol, 101 Kan. 557, 167 Pac. 1138, 1140; Denver Union Stockyard Co. v. United States [D. C. Colo.], 57 F. 2d 735, 748.)

[fol. 342] Counsel for plaintiffs contend that there should be included in the valuation of the Cities Service Gas Company $3,422,512 to cover initial cost of financing. This item was wholly disallowed by the Commission. We are of the opinion that the Commission's decision was right under the authority of Galveston Elec. Co. v. Galveston, 258 U. S. 388, 397, and Denver Union Stockyard Co. v. United States, supra, p. 742.

We conclude that that portion of the first order of the Commission, made August 31, 1932, that the distributing companies should give no consideration to the payments for gas at the city gates in excess of thirty cents per thousand cubic feet in fixing the rate for the domestic consumer, and the whole of the second order, made August 31, 1932, should be permanently enjoined; and that the temporary injunction against the attorney-general, being no longer necessary, should be dissolved.

Let decrees in accordance with the foregoing be prepared and submitted.

Orie L. Phillips, U. S. Circuit Judge. Geo. T. McDermott, U. S. Circuit Judge.

Hopkins, district judge, dissenting. Opinion later.

[File endorsement omitted.]

[fol. 343] IN UNITED STATES DISTRICT COURT

FINDINGS OF FACT—Filed Jan. 9, 1933

I

The citizenship and official position of the parties are as stated in the bills of complaint. There is diversity of citizenship in 1646-N, 1644-N and 1645-N, in which cases The Cities Service Gas Company, the Union Public Service Company and the Western Distributing Company are respectively plaintiffs. All of the cases involve a substantial federal question, and in each of the cases there is more than $3,000 in controversy.

II

On July 2, 1931, an order was entered by the Public Service Commission of Kansas, on its own initiative, directed to the plaintiffs herein except the Cities Service Gas Company, finding that the reasonableness of all contracts with, and charges made to, the respondents, by corporations owning the stock of the respondents, and of the contracts between Henry L. Doherty & Company and respondents, should be inquired into; the respondent distributing companies were ordered to show cause why payments made under such contracts, if found to be unreasonable, should not be disallowed as operating expenses. A copy of said order is Exhibit A to the bills of complaint of the distributing companies.

III

Pursuant to such order, extensive hearings were held. The properties of the Cities Service Gas Company, situated in five states, were appraised by engineers for both sides,

and valued by the Commission. The testimony and exhibits comprise many volumes; the expense of the trial, including the appraisement of the engineers, exceeded $300,000. On July 20, 1932, the Commission found that the payment of 13½ per cent of gross revenues made by the distributing companies to Henry L. Doherty & Company were unreasonable; that any rate paid by the distributing com- [fol. 344] panies to the pipe line company (the Cities Service Gas Company) in excess of 29.5 cents per thousand cubic feet for natural gas delivered to the mains of the distributing companies was unreasonable.* The distributing companies were ordered (1) to cease setting up on their books the payments of 13½ per cent to Henry L. Doherty & Company, and any payment for gas in excess of 29.5 cents per thousand cubic feet, and (2) to give no consideration to any such payments in fixing their rates to the domestic consumers, and (3) to reduce their rates to the consumers proportionately, pending a final determination of their rates; notice was given to show cause why such reductions should not be made permanent. A copy of such findings and order, with an elaborate supporting opinion, are attached to the bills by reference.

IV

A petition for rehearing on fifty one grounds was filed, and allowed as to one. Upon rehearing, a slight addition was made to the value of the properties of the pipe-line company, and the city gate rate was increased from 29.5 cents to 30 cents per thousand cubic feet. The order entered in July was again entered, this time as two orders; part (3) of the July 20th order, requiring a reduction in rates pending further hearing, was incorporated in a separate order. Upon the hearing of the application for a temporary injunction, counsel for the Commission confessed that part of the order to be invalid.

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*The city-gate rate is referred to throughout the record, and in these findings, as the "40-cent rate." That is the usual charge per thousand cubic feet for gas delivered to the mains of the distributing companies; local conditions lowered that rate to certain cities supplied by the pipe-line company, bringing the average down to the 39.5 cents referred to in the opinion and order of the Commission.

V

Except for qualifying shares, the common stock of the distributing companies is owned by the Gas Service Company, the stock of which in turn is owned by the Cities Serv-
[fol. 345] ice Company. The common stock of the Cities Service Gas Company is owned by the Empire Gas & Fuel Company, the voting stock of which in turn is owned by the Cities Service Company. The Empire Gas & Fuel Company has a preferred stock issue outstanding in the hands of the public. Henry L. Doherty & Company is Henry L. Doherty, who owns thirty five per cent of the voting stock of the Cities Service Company. The Cities Service Company, by stock ownership, legally controls the policies of the distributing companies and the pipe line company; and Henry L. Doherty in fact controls the policies of the Cities Service Company. The distributing companies do not deal at arm's length with either the Cities Service Gas Company or Henry L. Doherty & Company.

VI

The distributing companies, plaintiffs, are engaged in the distribution and sale of natural gas to domestic and industrial consumers. They operate in 128 cities and towns in Kansas. Their only dependable source of supply is the other plaintiff, the Cities Service Gas Company. Except for a few local gas fields of uncertain life, the distance of the gas fields from the localities served, and the cost of pipe line construction, are such that the Cities Service Gas Company has a practical monopoly on the sale of gas to the distributing companies. There is no agreement between the Cities Service Gas Company and the distributing companies as to the amount of gas that will be purchased; the oral agreement is simply that the pipe-line company will supply the present needs of the distributing companies at 40 cents per thousand cubic feet delivered to their mains.

VII

Prior to 1910, and during the years since then, Henry L. Doherty, doing business under the name of Henry L. Doherty & Company, has built up and now maintains a complete organization for the design, construction, operation
[fol. 346] and development of public utilities, oil and natu-

ral gas properties. This organization is composed of experienced executives, financial advisers, construction, valuation, electrical, oil and gas engineers, geologists, chemists, technicians, experts, accountants and operators. There are approximately 1,687 employees.

The same organization maintains departments for the purchase, sale, promotion and transfer of stocks of the various companies allied with the Cities Service Company; a foreign oil department; steamship and tank car department; an oil production and refining department; a real estate division chiefly concerned with New York real estate.

Each of the plaintiffs has entered into a contract with Henry L. Doherty & Company, by which the latter agrees to furnish the following services, subject to the control of the board of directors of the plaintiffs:

"I. Personnel. In so far as your corporation may desire, it is proposed to supply you with experienced executives and operators necessary for your business.

"II. Executive service. Our staff of executives, financial advisers, engineers and accountants will advise and assist in franchises, rates, matters of public relations, and all matters of insurance, supervise expansion of territory and business, acquisition of additional properties, etc.

"III. General accounting services. Our accounting department will periodically audit the books of your corporation and generally advise in accounting problems and in the developments in accounting practices and procedure, and furnish the services of certified public accountants where special audits are required.

"IV. Statistical services. Our statistical department will supply comparative statements of operating results of the various companies under our supervision and will also supervise or furnish statistical reports to financial institutions, government bureaus, and similar organizations.

"V. Purchasing services. We will give you the benefit of the services of our purchasing department with regard to [fol. 347] the purchase of equipment, supplies, generally advise as to the desirable equipment, etc.

"VI. Designing and construction engineering. Our engineering staff will be available at all times to carry out all preliminary investigations requisite to determining the advisability of any proposed construction, will check the

details of engineering design, perform engineering work where requested, and generally check the efficiency of your plant.

"VII. Financial services. The financial department will provide plans for financing and for funds for capital requirements, including construction and additions to properties and acquisition of new properties; for the refunding of maturing obligations; will act as paying agent for coupons and dividends, and assist in the arranging of bank loans. Also the financial department will furnish your corporation with a budget system for the advanced determination of financial requirements and operating results.

"VIII. Securities department. The securities department will provide plans for the sale and distribution of various securities, and will formulate and carry out campaigns for sales under customer ownership plans, etc.

"IX. Valuation. The valuation department will, when required, prepare inventories and appraisals of property, and will advise as to experts who may be required to testify in valuation cases, and will generally assist in the preparation of the same.

"X. Tax department. The tax department will prepare or supervise the preparation of federal and other tax returns and generally keep in touch with taxation problems.

"XI. New business department. The new business department will serve in the purchase and sale of appliances and equipment for resale, the determination of sales policies, promotion programs and sales personnel, in research and laboratory tests on domestic appliances, etc.

"XII. Technical and research department. The technical and research department will furnish a consulting service on all technical problems encountered by your corporation.

"Compensation. For the above services your corporation will pay as follows:

"1. A management fee equal to one and three-fourths per cent (1¾%) of its gross revenues, after deducting intercompany sales for resale.

[fol. 348] "2. An engineering fee equal to five per cent (5%) of the cost of construction.

"3. For the services of our securities department to purchase outright blocks of securities issued by your corporation or to distribute such securities to investors, we will charge a fee to be mutually agreed upon, depending on the character of security offered and general market conditions when the offer is made.

"In addition, your corporation will pay the expenses, disbursements and reasonable per diem charge for our representatives while at the properties of your corporation or traveling for it on special matters."

Payments received under these contracts are paid over to Cities Service Company, which in turn pays all the expenses of Henry L. Doherty & Company, without profit to Henry L. Doherty. The 1¾ per cent payment is not made on intercompany sales; that is, the Kansas consumer pays the 1¾ per cent but once.

VIII

The Gas Service Company, with offices at Kansas City, Mo., renders certain services to the distributing companies, for which a payment is made that is not here under review. While the same type of service is rendered under each of such contracts, there is no unreasonable duplication of service. Henry L. Doherty & Company furnish services which the Gas Service Company is not equipped to furnish. For example, the counsel and engineer employed by Gas Service Company can and do adequately handle the routine matters involving rates and service that arise in ordinary operations; they are not equipped to handle matters of the magnitude of this litigation; in such cases, the engineering and legal staffs of Henry L. Doherty & Company are employed. We find that this contract places at the disposal of the distributing companies engineering, legal, accounting, geological and business services of value, and of a character and extent which could not as economically be availed of by separate distributing companies or by any [fol. 349] small group of them; that similar contracts are made by other public utilities with similar organizations, such as Ford, Bacon & Davis, and Stone & Webster; that the propriety of such contracts is for the owners of the companies to determine.

IX

The activities of Henry L. Doherty & Company embrace many matters not covered by the 1¾ per cent contract, the expense of which is not a proper operating charge of the distributing companies. These activities are: the promotion, sale, and transfer of securities of the Cities Service Company and its affiliates. No securities of the distributing companies have been marketed by Henry L. Doherty & Company, and if they are, the contract provides for a separate fee for such services. The production, sale and transportation of oil, and the handling of New York real estate, are unrelated activities. The record discloses no reason for these distributing companies maintaining a London office.

The following activities of Henry L. Doherty & Company are or may be of direct benefit to the distributing companies:

Activities tending to increase the consumption of natural gas, by advertising and by development and marketing of gas-burning appliances; the geological department, the technical and research division; the tax, valuation and rate divisions; the purchasing department; the public utilities operating department; the department dealing with the training of personnel; the natural gas department; the corporate records department; the legal, engineering, accounting, auditing, finance and construction divisions.

X

The record discloses that the expenses of Henry L. Doherty & Company exceeded its receipts, over a ten-year period, in the amount of $1,768,440.26, the deficit being made up by the Cities Service Company. The expenses for [fol. 350] one year are classified, and from that classification a rough approximation of the expenses properly chargeable to the natural gas business is possible; something less than one-half of the 1931 expenses appears to have been incurred in activities not contemplated by the contract and not properly chargeable to operating expenses; certain large items, such as executive and office service, include the expense of both related and unrelated services. But the receipts are not classified. The utility business pays 1¾ per cent; the oil business 1 per cent; the

securities business apparently pays nothing directly, except that Cities Service Company makes up the deficit. But whether this is a fair division the record does not disclose, except that the deficit, over a ten year period ending in 1930, has been about 7 per cent, while the expenses of the securities business for 1931 were close to 30 per cent. It is therefore impossible to tell, from this record, anything about the pivotal question of whether the payments made by the distributing companies bear any fair relation to the expenditures properly made on their behalf. We cannot, therefore, find whether 1¾ per cent is too much or too little; it is probable that, until some segregation is made of departments, and perhaps a segregation of expenses within some of the departments, no accurate finding on this point can be made. If the entire 1¾ per cent is eliminated, the reduction of the average gas bill would be about ten cents a month. The record discloses that a part, at least, of such payment is proper. A finding of the amount thereof should be made, in the first instance, by the Commission.

XI

We find that it is of value to the distributing companies to have available a central organization equipped to render services of the character described by the contract, on demand; that the payment of the per diem charge, the per [fol. 351] centage on construction contracts, and the fee for the sale of securities, does not meet the expenses of such service, since much of the service is rendered without such specific charges. That whether such contract is advisable is for the officers of the distributing companies to determine. That the actual expenses of such services, if fairly allocated, is a proper operating charge.

We find it is not practicable to allocate with precision the cost of such general services to each distributing company, except so far as it is now allocated by the per diem and per cent charge in the contract. We find it practicable to segregate the cost of the services rendered to the public service companies engaged in selling gas, and perhaps electricity, to the public, from the cost of services rendered to companies engaged in the oil business, and from the expenses incurred in the promotion and sale of securities. The consumers of natural gas and electricity have no in-

terest in the oil or stock business, and such private business ought not to be thrown into a common pot with the business of serving the public, the expenses of all hopelessly intermingled, and then proportioned back to the public by those interested in the private business.

XII

The Cities Service Gas Company was organized in 1926. It took over the physical properties of five pipe line companies, having a plant investment account, at the time, of $[illegible]. These pipe line companies served many communities in Oklahoma, Kansas and Missouri. The companies taken over were integrated, so that gas could be run from the mains of one system into that of another, and the supply thereby made more dependable and economical. Natural gas had long been used for lighting and cooking in most of these cities and towns. Years ago gas had been freely used for heating, but the uncertainty of the [illegible] supply, caused in part by lack of capacity of the wells to meet the peak demands and in part by the frailties of the pipe line system, had driven the ordinary householder back to coal. The discovery of the extensive and prolific gas field at Amarillo, and later at Hugoton, Kansas, removed the first obstacle; large sums expended in new mains and in repair of old ones largely removed the second. The supply becoming again dependable, a vigorous campaign was waged for household heating and for industrial uses to absorb the excess in off peak seasons. The Cities Service Gas Company now has an adequate and dependable supply of gas, available at all times at the city gates. The Cities Service Company acquired the distributing companies in order to insure adequate service to the ultimate consumer, on the theory, doubtless, that a chain is no stronger than its weakest link. The service to the public is now sufficient and efficient. While these improvements in service were being made, electricity supplanted gas for lighting and is making serious inroads on the cooking, while fuel oil is proving a formidable competitor for heating. The original cost, or prudent investment, in the pipe line company's properties is somewhat obscure; the properties were acquired by a merger of other companies, whose original investment accounts cannot be

thoroughly checked. The probabilities are that the book cost of the properties is around $90,000,000. The system consists of 4,400 miles of pipe lines, 11 compressor stations, and 1,225,000 acres of gas leases, and gas wells on a part thereof.

XIII

There is no substantial dispute as to the inventory; the disagreement is over the present values of the properties. The valuations made by engineers for both sides, and by the Commission, is on the basis of cost of reproduction new, less accrued depreciation. The present values are, on the extensive constructions of the last few years, less than the prudent investment therein. Both engineers arrived at [fol. 353] the present per cent condition by inspection, although the amount of properties inspected differed somewhat. The engineers for the plaintiffs value the properties at $105,000,000; the engineers for the Commission, and the Commission, at $73,000,000. Approximately $22,000,000 of this difference is in four items gas leases, going concern value, cost of financing, and interest during construction. The remaining difference grows out of differences in valuations of the numerous items in the inventory. While this court has made an independent investigation of the facts, it has done so with the knowledge that the Commission had the benefit of hearing the witnesses, and that there is a presumption that their findings are correct. Unless, therefor, the record discloses some substantial reason to the contrary, the findings of the Commission have not been disturbed. The Commission apparently gave little or no weight to the factor of original cost, although when present values were higher than cost, great weight was accorded that factor by Commissions generally. We have found it unnecessary to explore the question of what weight should be given to that factor.

In the following findngs of value, the Commission's finding is adopted, because presumptively correct, except where there is an explanatory note.

XIV

The properties of the Cities Service Gas Company, used and useful in the public service as of September 1, 1931, are as follows:

1307	Production—Right of way*	$64,778
1327	Transmission—Right of way	1,915,427
1310	Production—Field measuring station structures	35,909
1311	Production—Other Structures	47,876
1312	Production—Gas Well Construction*	1,294,710
1313	Production—Gas Well Equipment	658,439
1314	Production—Field Line Equipment*	3,523,176
1315	Production—Field measuring station equipment*	265,746
1332	Transmission—Measuring station equipment	759,625
1316	Production—Drilling and cleaning equipment	27,908
1317	Production—Other Equipment	1,333
1325	Transmission—Land*	147,202
1328	Transmission—Compressing Station Structures*	1,515,662

[fol. 354]

1329	Transmission—Measuring Station Structure	133,310
1330	Transmission—Other Structures	113,341
1331	Transmission—Compressing Station Equipment*	8,463,835
1333	Transmission—Line Equipment*	40,232,331
1334	Transmission—Other Equipment	5,633
1376	General—Other Land	3,655
1379	General—Other Structures	94,687
1380	General—Office Equipment	106,035
1381	General—Store Equipment	1,805
1382	General—Shop Equipment	23,084
1383	General—Stable Equipment	568
1384	General—Garage Equipment	81,448
1385	General—Laboratory Equipment	8,202
1386	General—Telephone and Telegraph System	415,070
1387	General—Tools and Implements	44,979
1388	General—Other Equipment	21,832
	Engineering and Superintendence during Construction*	3,321,250
	Preliminary and Organization Expense*	500,625

Administration and Legal Expense during Construction	350,350
Miscellaneous Construction Expenditures	700,700
Taxes during Construction	875,171
Interest during Construction*	4,471,934
Working Capital	775,000
Materials and Supplies*	628,675
Gas in Line	22,000
Going Concern Value*	5,000,000
Gas Leases*	5,727,272
Rate Base	$82,380,583

1307-1327. (Mr. Black was the engineer for the Commission; Mr Hamilton for the plaintiffs. Both are engineers of standing.) The Commission allowed $1.40 a rod for right of way. It used $1.08 as a basis, that figure being the average cost, as shown by the books of the company, of 31 per cent of its rights of way. To this the Commission added 22 cents per rod for expense of acquisition, and 10 cents a rod for abstracts and recording fees. The evidence clearly developed that the figure of $1.08 did not purport to represent all of the costs, and it is not a dependable figure. The most dependable evidence is that of the man who negotiated for these rights of way during the past four years. His offering price, to all landowners, was 50 cents per rod for the land, and 50 cents per rod for damages; sometimes he paid as much as $2 per rod for the land alone; the average damage paid was 65 cents. He did not state the average cost for the land, but it cannot be assumed that he acquired all of it at his offering price. It should not be figured lower than 65 cents, the average [fol. 355] he paid for damages for which his offer was likewise 50 cents. These items make $1.30 per rod paid the landowner; adding to that the 32 cents allowed by the Commission for overhead, gives the figure of $1.62, which we have used. The company's figure of around $3 includes aerial surveys, which were not used, and if used, probably would have been worth their cost in a saving not reflected in its present valuation. Apparently the company also included certain construction costs elsewhere accounted for.

1312-1313. We have added two items to this joint ac-

count. The Commission deducted $57,235 from its engineer's valuation on a purely legal ground. It appears that in the Craig and Augusta fields the company uses dry holes, or played out wells, for storage; that is, excess gas from producing wells is turned into the dry holes, and the gas thereby stored for future use. It is not denied that the wells are properly used for storage, and for a public purpose; the claim is that the landowner has the property interest in the hole in the ground. Upon the trial before this court it was conclusively proven that the company has entered into gas leases, with royalties paid in advance, for the use of these wells. Its rights thereto are the same as in producing leases. The assumption of fact made by the Commission is erroneous; the legal conclusion need not be examined.

The other item is $84,318 growing out of the cost of gas-well construction. The company's figures were considerably below actual cost, and below the cost of adjacent wells drilled by other companies to the same depth. The engineer for the Commission omitted certain items in his calculations, which may account for his figures being so much below the actual cost of such construction. The Commission's figures are so far below the cost of these wells, or any other well in the vicinity, that they approach the arbitrary.

Counsel for the Commission suggests that the Commis- [fol. 356] sion's valuation is too high, because the per cent condition was computed on a straight line basis, whereas, in fact, as he says the gas wells depreciate more rapidly during their early years. None of the witnesses support this theory; it introduces a highly speculative element into an already troublesome problem; it is of no practical significance in this case, because the number of wells is large and of varying ages, and any theoretical error as to a single well is leveled out by the law of average.

1314. We have added $397,017 to this account. The Commission adopted Mr. Black's estimate, which was based on assumption that field lines were buried, on the average, to one-half the depth of main lines. The company's valuation was based upon the facts. Black testified his figures would have been more accurate if he had had time to gather the

facts. It clearly appears, also, that field lines are more expensive to construct than main lines; they are in smaller units; more hand labor is involved, and more connections are necessary; also the cost of field lines cannot be decreased by taking advantage of topograph, as may generally be done with main lines. The company's figures are strongly buttressed by an analysis of actual cost of field lines utilizing 20,600 tons of pipe. The assumptions of the Commission and its engineer cannot stand against the facts.

1315 1332. These accounts are treated together, and we find nothing from which to resolve the conflict between the engineers. The Commission rejected Hamilton's value because without supporting data; on rehearing the data was furnished, several volumes of it. It still leaves the conflict. We therefore use the Commission's valuation.

1325. We have added $2,000, the value of the land at the Hogshooter compressor station. The Commission eliminated this land, and the structure and equipment, on the [fol. 3574] ground that it was an abandoned station. The station is an old one, and has not been in use since 1925, because the gas fields supplying it were exhausted, and it was not so located as to serve other fields. In February, 1931, it was returned for taxes as an abandoned structure, at junk value. Since that date new gas fields have been discovered, and it is undisputed that the station is now strategically located, and plans and requisitions have been prepared to make the necessary alterations to put it back into immediate service. This undisputed evidence, corroborated by the physical facts, cannot be ignored because a tax return was made that at an earlier date it was abandoned. It is not now in service, except as an emergency station, but it is a component part of the system as it now exists. If eliminated now, a readjustment of the rate base would be necessary as soon as the work now requisitioned for is completed. We have restored this station to the rate base, using the valuation of the Commission's engineer.

1328. We have added the Hogshooter structure at Black's value of $49,560. We have not added the compressor stations at Owasso or Hominy. There is a difference of about $700,000 in the value of the structures at other compressor stations. Each engineer is corroborated by

contractors who estimated the cost of reproduction. The engineers and contractors testifying are all reputable and capable men. We therefore hold that the presumption of correctness attaching to the finding of the Commission has not been overcome.

1331. We have added the Hogshooter equipment at Black's valuation.

1333. The difference between the engineers' valuations of this item is about $4,000,000. The dispute narrows down to three items. (1) The Commission found the property to be in 90.1 per cent condition. The company asserts it to be in 92.93 per cent condition. The Commission's finding is supported by the testimony of its engineer and a con- [fol. 358] sulting engineer called by the company. We approve the Commission's finding as to per cent condition. (2) The cost of rock excavation. There was a dispute among the experts, but the Commission's finding is supported by the testimony of its engineer and a contractor who had done much of this work. Elaborate comparisons of costs of selected lines are introduced to show the error in the Commission's cost figure. But the results depend largely on the lines selected. While not entirely satisfied with the figure used, we are not disposed to disapprove the finding as to the cubic yard cost. (3) There is a difference between the engineers as to the amount of rock excavation in the lines. After the hearings before the Commission, engineers for both sides drilled a hole every quarter of a mile along a main 125 miles long. That extensive investigation developed that the percentage of rock excavation was 20.94 per cent instead of 10.46 per cent used by Black. If overcuts are included, the percentage is 28. We are inclined to believe that overcuts should be excluded; it is probable that contracts for trenches would be predicated on the trench debt, and would not call for overcuts caused by the inability to blast to a neat line. This additional evidence convinces us that Black's estimate of the amount of rock excavation is too low. His estimate on the line used for the test was 24,000 yards; Hamilton's was 72,482 yards. The test showed, on Black's own figures, exclusive of overcuts, 46,790 yards. The subject is not capable of exact proof, but we are of the opinion that Black's amounts of excavation should be materially increased. Mr. Hamilton's valuation of rock excavation is $4,211,120; Mr. Black's

$1,270,115, of which $1,154,503 is in this account. Applying Black's price to an increased amount indicated by the test, results in an increase of this item from $39,432,331 to $40,232,331.

Engineering and Superintendence is stipulated by the [fol. 359] parties to be 5 per cent of the value of the properties excepting accounts Nos. 1316, 1380, 1381, 1382, 1383, 1384, 1385, 1387, and 1388. The parties have stipulated that this and other overheads should not be depreciated. Accordingly we have computed overheads by applying the Commission's percentage to the undepreciated values of the property, using $66,425,000.

Preliminary and Organization Expense. We adopt the Commission's finding of ¾ per cent of the values of the physical properties; and for Administration and Legal Expense, ½ per cent on physical values including engineering; for Miscellaneous Construction Expenditures, 1 per cent, on same values. (See note.)

Interest During Construction. The Commission used a rate of 6 per cent; the company, 8 per cent. It is customary to calculate this item at the prevailing rate charged a person with good credit for temporary advances, which is now 6 per cent. This throws upon the borrower, the owner of the property, the hazard of the borrowed money during the construction period, which must be considered. Two per cent is a reasonable allowance for that hazard, but it is customary and preferable to make this allowance as a part of Going Concern Value. The parties have agreed that this item, as well as taxes, should not be depreciated. We have taken the Commission's figure, increased by 6 per cent on the difference in values found, approximately $200,000.

Materials and Supplies. Commission's figure plus its allowance of $119,275 on rehearing.

Going Concern Value. Mr. Hamilton's estimate of going concern value is $8,898,532. Ford, Bacon & Davis valued this item from $8,500,000 to $9,000,000. The engineer for [fol. 360] the Commission valued it at $3,820,000. The

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Note.—We accept the Commission's finding, instead of the stipulation of the parties, because the Commission's finding is in accord with the record, and there is an acknowledged error in the stipulation.

Commission allowed $2,000,000. Counsel for the Commission urges that nothing be allowed.

That such a value exists is acknowledged by all engineers and appraisers, and is a matter of common knowledge. That allowance therefor cannot be denied because of difficulty in evaluation, is settled by decisions of the Supreme Court of the United States and of the Supreme Court of Kansas. Many items enter into it. There is a value to records that have been built up, and to a personnel that has been trained. The period of construction was two years. Physical deterioration went on during that period when there were no earnings to offset it. The owner's money was embarked in a hazardous enterprise during the construction period; the Commission allowed only 6 per cent for interest during construction on the theory that an owner, with good credit, could borrow money at that rate. But the owner should be compensated for the risk involved in putting his credit back of the enterprise. If 8 per cent is a fair return on moneys embarked in this business, as we elsewhere find, that hazard was present during the construction period. The difference between 6 per cent interest during construction and an 8 per cent return in a business venture during construction, is $1,450,645, based on the Commission's valuation. During the construction period, there are no revenues, and depreciation and return (less interest during construction) must be capitalized in going concern value. After construction is completed, and some business is attached, there is an idle investment until the available business is fully attached, even under the most efficient management. It would be foolish, of course, to construct a pipe line capable only of taking care of the needs of to-day, with no provision for the reasonably anticipated needs of to-morrow. The Commission recognized this in another part of its opinion, when it stated:

[fol. 361] "Further, as pipe line extensions were developed, they necessarily were not fully productive until the volume of sales had been built up to the capacity of such extension. A large proportion of the investment each year was unproductive, although the investment has been included in the plant investment values included in the above, and will be included in the future. This discussion relative to idle plant is merely for the purpose of illustrating that the company has been earning a high return not only on

its production property but on its idle and non productive property."

The Commission's theory that rates for the future should be discounted because of the profits of the past is not sound law. Values cannot be increased by capitalizing past losses; (Georgia Ry. v. R. R. Comm., 262 U. S. 625, 632) the corollary that they cannot be decreased by reason of past profits, is equally well settled. (Board of Commrs. v. N. Y. Tel. Co., 271 U. S. 23, 32.) Counsel for the Commission assume, contrary to the finding of the Commission, that the business existed when the lines were constructed. The town existed; the distributing companies existed; there was a market for some gas. But, like every other utility, the market had to be and was developed. Vigorous campaigns, in part successful, have been and now are being carried on to develop the market, particularly for house heating and for industrial gas to utilize the surplus in off peak periods. It is no answer to say that these campaigns are carried on by the distributing companies; no matter who developed the market, the fact is, as testified to by the engineer for the Commission, and as found by the Commission, a part of the plant was necessarily idle while the market was being developed. The Commission's engineer testified:

"I have taken as the best measure of certain items of that going value the company's operating experience, and briefly I have allowed in arriving at this figure used herein, $15,000.00 for the books and records of the company, I have allowed $1,020,000.00 for organization of the operating company, that is the organization of the company, and I have allowed interest and depreciation on idle plant, plant [fol. 362] that would be idle during the period this company is acquiring its business, that is between the end of the construction period and the time all business is attached, in the amount of $2,784,645.00, added to the two other amounts of $15,000.00 and $1,020,000, gives $3,819,645.00, which I have applied as $3,820,000.00."

While Mr. Black allowed depreciation and return on idle plant while the company was acquiring its business, in the amount of $2,784,645, no similar allowance apparently was made during the construction period. The difference between 6 per cent interest allowed and an 8 per cent return is $1,450,000. The parties agree on the Commission's fig-

are of 2.90 per cent annual allowance for depreciation. Allowing half of that for the two-year construction period, adds approximately $2,715,000. Without undertaking any precise evaluation of this intangible asset, it is difficult to see how it can be fairly approximated at less than $5,000,000 which is about 5 per cent of the tangible values, a much lower percentage than the percentage customarily allowed.

Cost of financing, valued by the company at $3,422,512 was disallowed by the Commission; we approve, on the authority of Galveston Elec. Co. v. Galveston, 258 U. S. 388, and Denver Union Stockyard Co. v. United States, (D. Colo.) 57 F. 2d 735, 742, and cases there cited.

Gas Leases. The company owns the gas rights in about 1,261,000 acres, of which 42,297 acres are developed; 196,170 acres proven; 25,667 are in probable territory; and 998,287 acres are classed as of prospective value only.

Many experienced witnesses, testifying for the plaintiffs, valued these leases at figures, the average of which is $12,914,189, of which $1,996,574 represents the 998,287 prospective acreage. Mr. Holl testified for the Commission as to values; he was a practical geologist and oil man, with [fol. 363] no personal knowledge of the fields in question; and no particular experience with gas leases. His testimony was predicated on a trip he made to the fields for the purpose of testifying, and inquiries made on that trip. He valued the leases at about one third of the company's value. The Commission valued them at $3,279,237 of which $998,287 was for prospective acreage. The Commission valued the Amarillo holdings at $4,281,894; the Hugoton holdings at $556,116. The cost of the leases, after deducting those bought for the Texoma Company, was $5,727,272.

The Commission excluded all but 71,267 acres from the rate base. The holdings of the company at Amarillo alone are 94,820 acres. The acreage allowed is valued by the Commission at $2,874,390. The Commission arrived at this result by finding the amount of gas left in the Amarillo holdings, based upon the estimate of geologists; it deducted from the company's requirements, gas now being purchased by the company from other producers; and found that the gas in the acreage allowed would serve the customers for 22 years.

The Commission found that the remaining leases were acquired for speculative purposes, a finding based upon

one fact: the Texoma Company was formed by the Cities Service Gas Company and other interests to build a pipe line to Eastern states; leases were acquired by the Cities Service Gas Company for its affiliate, and later transferred to it. On the other hand, in this court, is the uncontradicted sworn statement of responsible officials that all the acreage was acquired as gas reserves for this pipe line. There is also the significant circumstance that not a single lease, acquired for that purpose, has been sold. We hold therefore, that these leases were acquired, and are held, in good faith, for this pipe line, and that the findings that they are held for speculative purposes is contrary to all the evidence.

We further find there was error in eliminating these leases from the properties of the company because the company is now contracting some gas, and conserving its [fol. 364] own. The first duty of the company is to see to it that its patrons have an adequate supply of gas. To insure this, it must own the gas. Contracts for gas are well enough when gas is plentiful, but when the shortage comes, contracts are not adequate safeguards. Broken contracts will support verdicts for damages, but they will not heat the houses nor cook the breakfasts of the patrons in Kansas. The company has not only the right, but is under the duty, to own enough gas to meet the needs of its customers.

Who shall determine what reserves are adequate? A Commission, with no moneys invested, or the owners of this pipe line which, without gas, is worse than useless? Within the limits of reason, undoubtedly that determination must be left with the owners. Perhaps they have been over-cautious, but if error is to be made, it should be on the side of ample reserves. The owners of this property had seen the gas exhausted from field after field; they had seen their customers lost because the supply had failed; they had seen fields of great promise belie their expectations. They had seen geologists wrong before. In recent years they had seen the state prorate the taking of gas. The Commission's figures are predicated on a 20 per cent recovery; within two weeks of its order, the Texas Railroad Commission cut this to 4 per cent. What the future may hold, by way of state action, no one knows. We cannot say the owners did not, in good faith, acquire this acreage to protect their great investment and to insure their patrons a de-

pendable gas supply. They invested around $4,500,000 in 200,000 acres in proven or probable territory, and about a million more in a million acres in prospective territory. Upon this five and a half million investment depends the entire value of $75,000,000 of pipe lines and many more millions in the properties of affiliated distributing companies. The Hugoton field is not now connected with the pipe line; but it is a field of great potential supply, is fa- [fol. 365] vorably situated, and the investment therein is not large. We find that all the acreage owned is used and useful in the public service.

The value of it is problematical, as is true of all gas properties. If the Amarillo field stands up, it is probably worth the value placed on it by witnesses for the company; if it stands up, then that field is adequate for the needs of twenty years; it may not stand up, and the company acquired Hugoton and other acreage against that eventuality; if it does not, it is not worth so much. Its value depends upon a future market, and on the actions of state commissions. The overwhelming weight of the competent evidence sustains the valuation of the company, around $12,000,000. That is about twice its cost. For the purpose of this case, and upon the authority of United Gas Co. v. Railroad Commission, 278 U. S. 320, we have put the gas leases in at cost. The figure is arrived at by subtracting from the cost of all the leases, the cost of those transferred to Texoma, which leaves the cost of those now held.

XV

Equally efficient substitute. The chief engineer for Ford, Bacon & Davis testified that the present cost of a pipe line from the gas fields at Amarillo to the cities served by the Cities Service Gas Company, together with the cost of acquiring adequate gas reserves, would be $91,500,000. That in making this estimate he had assumed that the lines could be constructed as the crow flies, and he did not take into account the actual topography of the country; that the lines were designed as cheaply as could be, and that such a system would not furnish the same quality of service as is now furnished by the present pipe line. Applying the 90 per cent condition of the present system to the physical properties of this hypothetical substitute, would reduce this

figure approximately $7,000,000 (computing $70,000,000 as cost of depreciable properties in hypothetical line), or a present value of $84,500,000.

[fol. 366] XVI

The revenues which can reasonably be anticipated from the properties of the Cities Service Gas Company under the present rates, are as follows:

Annual net operating income*		$8,401,680
Depreciation of physical properties, at agreed figure of 2.96%	$1,966,180	
Rentals on nonproducing leases*	329,917	
Dry hole expense*	174,747	
Depletion of producing leases (agreed)	70,509	2,541,353
Net available for return, or 7.11%		$5,860,327

Operating income. Except for two items hereinafter noticed, operating expenses are not questioned. The record discloses operating income for the two years ending June 30, 1931, and June 30, 1932; and also for the year ending December 30, 1930, but this year involves a six months overlap into the June 30, 1931 year, with no way to apportion it. We have accordingly taken the two separate years shown. The income for 1932 was $880,000 short of 1931. We agree with the Commission that 1932 should not be taken as a test year, for it marks, it is hoped, the low of the depression through which we are passing. The 1932 figure of $7,861,516 includes an item of $52,297.13 paid under the 1¾ per cent contract, which the Commission disallowed. It also includes an item of $50,000 being a portion of rate case expense of $250,000, amortized to that year. The Commission taxed $66,936.08 as costs to the respondents. The Commission, not challenging the amount, deducted it as a non-recurring expense. But the court records show that rate cases constantly recur. The city-gate rate for gas, serving the cities involved in this case, has been almost constantly in court for nearly twenty years. Extraordinary rate expenses should be amortized and allowed for the reasons set out in Denver Union Stockyard Co. v. United States (D. C. Colo.), 57 F. 2d 735. The $50,-

000 calculated in but one of the test years, is an estimate that $25,000 a year of such expense may be expected. We [fol. 367] have averaged the two years shown (adding the 1¾ per cent payment to each year) and adopted $8,401,680 as the anticipated revenues for the future.

The Commission still further increased this, by assuming that the income of 1931 was earned upon a lesser investment in the properties; accordingly, the Commission deducted from its value as of September 1, 1931, net additions to capital as disclosed by the company books from January 1, 1930, to September 1, 1931. But this is shown to be inaccurate, because additions were not charged to capital until long after the addition was in service; a lag of from one to three years was customary, in order to close up all claims growing out of a particular job. During 1931 there was almost no construction; there was some during 1930, but part of that was to replace existing facilities. There is evidence that there were not to exceed $2,000,000 additions to plant in the test period; and this would be more than offset in the decline of values between 1930 and the date of the valuation. The properties upon which a return is allowable are those actually in public service at the time of the valuation, and not an average of values theretofore existing. Income for the past, used as a guide for the future, should be figured against property in service when the income was earned; but the facts are, without contradiction, opposed to the Commission's assumption in this regard.

To this income the Commission added a sum for construction credit which it is now stipulated is in error; and also an item of $23,310 for income tax accruals in the calendar year of 1930, the origin of which is not clear. Income tax is an operating expense. Galveston Electric Co. v. Galveston, 258 U. S. 388. This appears to be an excess accrual over the amount finally determined to be owing for the year; if so, it means the operating expenses for the year are too high; but the record does not show whether it is already [fol. 368] deducted in arriving at the stipulated "net income." If it was not deducted, the stipulated figure is not "net income" as it says it is. The item is not of particular significance; only half of it is applicable to the last six months of 1931; and averaging that with 1932, reduces the item to about $5,000; we have assumed the stipulation speaks the fact, and have dropped it out.

Addition was also made because of payments on account of the 1¾ per cent contract on gas sold to others than the plaintiffs. Part of this expense is justifiable, particularly since the Cities Service Gas Company has no such agreement as the distributing companies have with the Gas Service Company. But the justifiable amount is not proven, and we accordingly add this payment to the operating income of each of the two years.

Depreciation allowance. The Commission found the weighted average per cent for depreciation of physical properties to be 2.96 per cent. This percentage should be applied to the undepreciated values of the physical properties for the reasons set out in State v. Southwestern Bell Tel. Co., 115 Kan. 236, 292; we have treated as depreciable properties those which the parties stipulated as the base for computing engineering and superintendence, $66,425,000. No allowance is made for overheads which the parties agree should go into the rate base undepreciated, for manifestly no annual allowance is necessary for nondepreciable properties. In so doing, we express no opinion as to whether the parties applied correct principles in arriving at their agreement.

Rentals on nonproducing leases. The Company claims a general development expense of $532,530.77, which includes rentals on nonproducing leases, and scouting and geological expense. The latter items enter into the rate base, and there is no proof that such expense will be necessary in the future to increase the already ample reserve supply of gas. Lease rentals are proper, and the Commission allowed rent- [fol. 369] als on 1,060 acres of nonproducing leases. Having determined that the company properly owns a large reserve, the lease rentals must be allowed.

Amortization of nonproducing leases. This point can be best illustrated by an example: Assuming a bonus of $1,000 is paid for a lease not yet producing. We have allowed its value in the rate base, and rentals paid thereon as an expense of operation. When it produces, depletion is allowed. The company amortizes the $1,000 over the life of the lease, presumably about five years, because producing leases are of indeterminate life. If a nonproducing lease, like a motor car, is a depreciable item, the cost should be amortized. But a nonproducing lease is not depreciating, any more than any other real estate, save that it may be

surrendered if found to be nonproductive. When and if it is surrendered, the cost must then be charged to operations or amortized. But should it be amortized before it is developed or surrendered? The question is very doubtful; there is no clear evidence that the 1930 figure of $314,981.68 is apt to be a necessary expense for 1933 and 1934. Accordingly, with hesitation, we disallow the item.

Dry hole expense. The Commission assumed that one dry hole a year would be all that would be suffered in an orderly development of this vast property. The actual expenditure in the test year was $174,747.74, a sum representing the cost of ten or eleven dry holes. The facts must govern. The company is not needlessly drilling dry holes, and geology has not reached the point where only one dry hole a year can reasonably be anticipated by a company owning nearly a million acres of prospective leases, scattered in three states and many fields.

XVII

Under the present rates, the Cities Service Gas Company is earning 7.11 per cent a year upon the present value of its properties.

[fol. 370]

XVIII

A return of approximately 8 per cent upon present values is necessary, under present conditions, to assure confidence in the financial soundness of the Cities Service Gas Company, to maintain its credit, and to enable it to raise money necessary for the discharge of its public duties. Any return substantially lower than that would be confiscatory. (United Railways v. West, 280 U. S. 234, 252.)

Rate of return. The pipe line company is subject to the hazards attendant upon the production of gas, and its transportation to distant markets. The amount of gas it may take from is own wells; and the price it may charge for its product, is subject to regulation by public authority. It must find a market in a highly competitive field. It competes with coal and fuel oil in household heating and for industrial purposes; the competition of fuel oil is particularly formidable for household heating; improved oil burners are automatic, approved by the National Board of Fire Underwriters for safety, are as clean as gas, and dependable. Electricity has

absorbed the household lighting and is making serious inroads on cooking. In short, it must search for and find its gas; transport it hundreds of miles without an hour's interruption; then find and satisfy its customers. The law contemplates that it make no more than a fair return in good times; it should not be forced to take less, when times are hard. There is evidence that in years past, the profits of the company exceeded 10 per cent. We do not analyze those figures; in rate making, the past must bury its dead; a confiscatory rate cannot be ordered for the future because an exorbitant profit was made in the past. (Georgia Ry. v. R. R. Comm., 262 U. S. 625, 632; Board of Commrs. v. N. Y. Tel. Co., 271 U. S. 23, 32.)

What is a proper return is a question of fact in which the elements of time and place play an important part. In this part of the Middle West, it is a recognized fact that in normal times, public utilities must promise a return of approxi- [fol. 371] mately 8 per cent, if capital for construction and extensions is to be attracted from other investments. The Kansas statutes recognize 8 per cent as a minimum return for waterworks property (sec. 13-1201, R. S. Kan. 1923) and provide for a recapture of a portion of the earnings over 10 per cent of gas and electric companies (sec. 13-1204, id.). The Kansas supreme court has held that earnings from 8 to 9 per cent on telephone properties are reasonable. (The State, ex rel. v. Telephone Co., 115 Kan. 236.) The witness for the Commission testified that 8 per cent would not be an unreasonable return in normal times, but testified that these times are abnormal, as they are. But if abnormality is considered, the return must be increased, not decreased. In these times, when stock of the best utilities can be purchased on a 9 per cent basis or better, certainly an 8 per cent return on this hazardous enterprise is not unreasonable.

XIX

The order of the Commission would reduce the net revenues of the Cities Service Gas Company by $1,926,145.07. (The amount is stipulated.) Under that order, the return upon the properties dedicated to the public use would be 4.8 per cent, which rate is confiscatory.

XX

If the distributing companies are compelled to pay 40 cents per thousand cubic feet for gas at the city gates, and to base their rates to the consumers upon the price fixed as reasonable by the Commission, no one of them will have earnings in excess of operating expenses, applicable to depreciation and return.

XXI

The distributing companies could not continue their business and pay the Cities Service Gas Company 40 cents per thousand cubic feet, and predicate their rates to the consumers upon 30 cents; the Cities Service Gas Company could not continue its business without the patronage of the distributing companies.

[fol. 372] Conclusions of Law

I

That *portion of the* first order of the commission, made August 31, 1932, that the distributing companies should give no consideration to the payments for gas at the city gates in excess of thirty cents per thousand cubic feet in fixing the rate for the domestic consumer, and the whole of the second order, made August 31, 1932, should be permanently enjoined.

II

The preliminary injunction against the attorney general should be dissolved; its purpose has now been subserved; the permanent injunction will enjoin all officers of the state from undertaking to enforce, directly, or indirectly, the orders herein held void.

III

The costs in this court should be assessed, one-half to plaintiffs and one-half to the defendant Commission.

Orie L. Phillips, Circuit Judge; Geo. T. McDermott, Circuit Judge.

[File endorsement omitted.]

[fol. 373] In United States District Court

Supplemental Memorandum. Filed Jan. 16, 1933

We are advised that a misunderstanding exists among counsel as to the scope of the opinion and findings as to a reasonable return, a misunderstanding doubtless contributed to in part because the court acceded to the suggestion of counsel that findings be made as to all controverted issues, and in part by differing conceptions as to the elasticity of the words "substantially" and "approximately." While supplemental memoranda often confuse instead of clarify, an interpretative resume may not be amiss.

A "reasonable rate" is not a particular decimal. A "reasonable rate" is one that falls within the zone of reason; it is a field, and not a mathematical point. The lower limit of the zone of reason is confiscation, that is, a denial of a net return sufficient to preserve the property and to attract capital necessary to enable the utility to discharge its public duties. A finding that a particular rate is reasonable, is not, therefore, a finding that every other rate is either unreasonable or confiscatory.

With the determination of the proper rate within that zone of reason, the courts are not concerned, for that is a legislative matter. As jurisdiction is invoked here, and generally in such cases, the courts decide but one question: Does the prescribed rate fall below the lower limit of the zone? The rate order in this case allowed a return of 4.8 per cent on the fair value of the property. The issue tendered is the validity of that order. We have held, and hold, that such order is confiscatory. Except in rough approximation, and by way of recital of evidence in the record, we have not undertaken to fix with precision the lower limit of this zone of reason.

Orie L. Phillips, U. S. Circuit Judge. George T. McDermott, U. S. Circuit Judge.

[File endorsement omitted.]

[fol. 374] IN UNITED STATES DISTRICT COURT

DISSENTING OPINION—Filed Jan. 14, 1933

HOPKINS, District Judge, dissenting:

There are suits in equity to enjoin the enforcement of certain orders of the Public Service Commission of Kansas. The questions presented involve the reasonableness of certain contracts between various of the Henry L. Doherty operating corporations.

The facts so far as necessary to this discussion are these:

One of the Doherty Companies, the Cities Service Gas Company, conveys from the gas fields and furnishes gas to the local distributing companies at the various city gates at a contract price of 40 cents per thousand cubic feet. Under another contract each of the distributing companies pays to Henry L. Doherty, doing business as Henry L. Doherty and Co., these items: one and three fourths per cent of its gross revenues, a per diem, an expense charge for certain specific services and an engineering fee of 5 per cent of the cost of construction.

July 2, 1931, the Public Service Commission upon certain findings therein made, entered an order for a hearing to inquire into the reasonableness of such contracts.

The respondents appeared and after a hearing and rehearing the commission, on August 31, 1932, entered an order substantially to the effect "that on and after the 1st day of September, 1932, the distributing companies shall cease to set up on their books as an expense item any payments made to Henry L. Doherty and Co., of the 1¾ per cent charge and also any payments made for main line town border gas in excess of 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer."

The instant actions were commenced September 19, 1932, to enjoin the enforcement of such order. The bills alleged [fol. 375] diversity of citizenship, that the orders were confiscatory of the property of the plaintiffs, impair the obligation of their contracts, deny to them the equal protection of the law, and unconstitutionally interfere with interstate commerce.

The cases were consolidated for trial. Upon the trial here the same evidence introduced before the commission was received, supplemented by an agreed abstract thereof, an agreed statement of facts and by stipulation and other evidence. These cases are a sequel to Western Distributing Co. v. Commission, decided by this court in 1931, and affirmed by the supreme court February 29, 1932 (285 U. S. 119).

At the threshold of this inquiry we are met by six propositions which must be kept in mind throughout the investigation:

1st. Natural gas is one of the great natural resources. It is discovered, extracted from the earth, transported and sold to the people of a hundred and twenty-eight cities and towns involved in this inquiry. The respondent has secured control of this great resource for which the people must now pay.

2d. That while the problem in this territory a few years ago was one of finding gas to supply the demand, it is now a question of finding a market for what appears to be an almost inexhaustible supply.

3d. That the Henry L. Doherty organization is perhaps one of the most efficient ever known, engaged in the handling of public utilities and products thereof, for which reason it has good credit and is enabled to borrow necessary funds for its operations at the lowest available rates.

4th. That within the past two and a half or three years utility rates in this territory have perceptibly fallen and that a return of from five to seven per cent is now equal to the purchasing power of from seven to ten per cent during the period of prosperity just preceding that time.

[fol. 376] 5th. That it is a matter of common knowledge that the Doherty organization has been and is selling and offering to sell gas to individual consumers in this territory, not only for industrial, but for domestic purposes, at rates far below the thirty-cent rate fixed by the public service commission to the distributing companies at the city gates.

6th. That while public utility rates in general throughout this territory have been perceptibly lowered during the last two or three years, the Doherty forty-cent rate at the city gates, has remained the same.

The commission contends that the order under inquiry is not subject to the constitutional objections urged by the

plaintiffs because it finds only that the contracts are unreasonable and that the extent of such unreasonableness. I do not agree with this contention. The order expressly prohibits payments made to Henry L. Doherty & Co., and to the Cities Service Gas Co., for gas at the city gates in excess of the thirty cents per thousand cubic feet "in fixing a rate for the domestic consumer," on and after September 1, 1932. The order, in my opinion, would affect the rates charged the domestic consumers and is in fact a rate-reducing order, and is therefore subject to review.

There is no contention on the part of the Commission that it has power to regulate interstate gas rates. However a state does have the power to regulate the price of gas brought into it and sold directly to the consumer, because "the business of supplying local consumers is a local business, even though the gas be brought from another state" (Missouri v. Kansas Gas Co., 265 U. D. 298, 309; Penna. Gas Co. v. Public Service Comm., 252 U. E. 23; East Ohio Gas Co. v. Tax Commission, 383 U. S. 465).

In spite of a stipulation between the parties, I do not concur in the view that if the charge made by the plaintiff at the city gates was reduced to thirty cents it would result [fol. 377] in a reduction of $1,926,000 in its net income. In all human probability a reduction in rates would induce a greater demand for gas. The plaintiff states that other fuel costs have been reduced. For instance, at page 104 of its brief it says:

"In 1924 and 1925 many of these distributing companies were acquired by the Cities Service organization and at no time from then until now has there been any failure in service. Natural gas in this territory does not have as many outages as does electric service which is always taken as the ideal service in the utility field at which to aim. The best evidence in this improvement in service is shown by the annual reports to the Public Service Commission which show the *increased annual sales of gas per customer in all of the towns in this territory throughout the last six or seven years, notwithstanding the fact that during this period the cost of competitive fuels was steadily being reduced, coal and oil now selling at prices hitherto unknown.*"

At page 106 it says (on the question of interest rates):

"No changes in gas rates from 1922 to date have been made except reductions. These distributing companies have not yet recovered from the effects of their experience as isolated companies to an extent whereby they are able to furnish their own financing for extensions and betterments at a reasonable cost. But they have at all times been furnished with whatever money was needed for additions and betterments by the Cities Service Company and they have been charged an *interest rate of only 6 per cent for this money.*"

But the 40 cent gas rate has not been reduced. Nor do I concur that a rate of 8 per cent upon present values of the plaintiff is necessary under present conditions to secure confidence in its financial soundness, or to maintain its credit and enable it to borrow money.

I do not assent to the conclusion that forty cents per thousand cubic feet at the city gates is a reasonable charge and that to compel the plaintiff to furnish such gas at thirty cents per M. C. F. will result in confiscation of its property.

I concur in the view of the majority that the various [fol. 378] Doherty companies are engaged in a common enterprise and that the principal one, the Cities Service Company, is through the agencies of the other corporations, supplying gas to the local consumers and is therefore engaged in a local business. The fact is that the Henry L. Doherty organization is one of the most efficient, far reaching monopolies operating in this country. It has many interlocking corporations. The common stock of the Cities Service Gas Company is owned by the Empire Gas & Fuel Company, the voting stock of which in turn is owned by the Cities Service Company. Henry L. Doherty & Co. is Henry L. Doherty, who owns 35 per cent of the voting stock of the Cities Service Company and controls its policies. The Cities Service Company, by stock ownership, legally controls the policies of the distributing companies and the Cities Service Gas Co. Henry L. Doherty in fact controls the policies of all the interlocking companies.

Since as far back as 1910 Henry L. Doherty, doing business under the name of Henry L. Doherty & Company, has been completing and building up this organization. It is

manned by experienced executives, financial advisors, construction, valuation, electrical, oil and gas engineers, geologists, chemists, technical experts, accountants, operators and lawyers. All are men high in their various professions. Through the years they have learned the Doherty way. They see through the eyes of Mr. Doherty, understand the Doherty language, ("their master's voice,") and speak the voice of Mr. Doherty. This is not said in criticism of the Doherty organization, nor of the men high in their professions and avocations, who manage and direct it, but only to illustrate this efficient, powerful, operating machine known as the Doherty organization. With due credit to the poet Pope, it may be observed:

"That all are parts of one stupendous whole,
Whose body many corporations are, and Doherty the soul."

I also concur in the view that since the Doherty compa- [Fol. 379] nies exercise a monopoly for supplying gas to the various communities served by the distributing companies, parties herein, and since the Cities Service Gas Co., is the unit which procures, conveys and delivers the gas to the other companies, that the only method of determining the fairness and reasonableness of the charge at the city gates is to determine the reasonableness of the return to the Cities Service Gas Co., on its property used and useful in such business.

I further concur in the view That in determining the facts, the findings of the Public Service Commission are presumed to be correct (Blanton v. Belt Line Ry. Corp., 268 U. S. 413, 422; Cotton v. Kansas City Stockyards Co., 183 U. S. 79; Denver Union Stockyard Co. v. United States [D. C. Colo.] 57 Fed. 2d 735, 739), and that, on the question of confiscation, the plaintiff is entitled to the independent judgment of a judicial tribunal as to the law and facts. (United Railways & E. Co. v. West, 280 U. S. 234, 251; Blue Field W. W. & Imp. Co. v. Public Service Commission, 262 U. S. 679, 689; Ohio Valley W. Co. v. Ben Avon Borough, 253 U. S. 287; Lincoln Gas Co. v. Lincoln, 223 U. S. 349; Crowell v. Benson, 285 U. S. 2269.)

A contention that the commission is not concerned with the future is not well founded. It is settled that the Commission is concerned with rate for the future, and the ex-

perience of the past is the only criterion by which it may make rates for the future.

The history of this company shows rapid development since 1926, when taken over by Mr. Doherty, as to investment in plant increase, in sales of gas and in net income. For instance, gas sales in 1927 amounted to $10,771,491; in 1930 $15,380,609, an increase of 42.79 per cent. Investment in plant increased from December, 1927, to December, 1932, 50.23 per cent. During the same period net earnings increased 65.48 per cent. During this period what is known as the Amarillo Wichita Ottawa line was completed, and extensions were made of major importance to Nebraska [fol. 380] and Missouri, developing new markets for the business. In 1930 the effect of the depression began to affect sales and earnings of the company largely through loss of industrial business, a business bound to be regained as industrial business improves; and it goes without saying that the carrying of the investment and expense of industrial business should not be placed on the domestic consumers.

Sale of gas for drilling and field purposes during 1932 period were only 36.55 per cent of such sales during 1930 (showing abnormality during 1932) and it is reasonable to expect that with the return of activity in the oil and gas business the markets for drilling and field gas will be revived.

Earnings should be averaged over a reasonable period of time in order to determine whether a utility is earning a fair return, or more or less than a fair return, for rate making or any other purposes. (Denver Union Stock Yards case, supra.) "The only fair test is to level out the peaks and valleys and estimate the future according to the mean line." Complaint is made that the commission used an average value. The same reasoning which requires the use of average earnings requires the use of average values. It is not fair to compare earnings during 1929 and 1930, with the values in 1931 and 1932, when there were extensive additions to plant investment. The use of average values contemplates the inclusion of values averaged over the same period used for the averaging of earnings.

In connection with the specific questions raised are general questions of public policy. This organization has secured control of a great natural resource for which the people must pay. The question for determination is what

charge constitutes the rate base for this plaintiff in arriving at a fair value of its property and what would be a reasonable rate to charge for the product and services rendered to the people. How shall the people of these hundred and twenty eight cities and towns be permitted to enjoy this natural resource free from extortion and at the same time allow the utility a fair return on the value of its property? [fol. 381] The showing must be clear before the court should interfere with the commission's order. Especially is this true where no actual experience has been had of the practical result of the rates fixed. While there is an alleged prophesied loss of income from a reduced rate, it must not be overlooked that such reduction means probably increased consumption.

In Wilcox v. Consolidated Gas Co., 212 U. S. 41, it was said:

"Where the rate complained of shows in any event a very narrow line of division between possible confiscation and proper regulation as based upon the value of the property found by the court below, and the division depends upon opinions as to the value, which differ considerably among the witnesses, and also upon the results in the future of operation under the rate objected to, so that the material fact of value is left in much doubt, a court of equity ought not to interfere by injunction before a fair trial has been made of continuing the business under that rate, and thus eliminating, as far as is possible, the doubt arising from opinions as opposed in facts."

. . . . . .

"There is no particular rate of compensation which must in all cases and in all parts of the country be regarded as sufficient for capital invested in business enterprises. Such compensation must depend greatly upon circumstances and locality among other things, the amount of risk in the business is a most important factor, as well as the locality where the business is conducted and the rate expected and usually realized thereupon investments of a somewhat similar nature with regard to the risk attending them."

F. C. Hamilton and E. B. Black were the principal engineers testifying in this case. Both are eminent in their profession. Mr. Hamilton for many years a member of

the Doherty organization learned in that organization's activities, knowing its business, being interested therein, naturally an efficient and proficient booster of its values when rate matters are involved. All this may be said without in any manner impugning the ability or high character of Mr. Hamilton. It only directs attention to the fact that he has been for many years and is interested in the success of the Doherty organization. That his education and environment have all developed a viewpoint [fol. 382] which necessarily is for the benefit of the utility. That he is an interested witness.

Mr. Black is an independent engineer, a member of the old firm of Worley & Black, now Black & Veatch, of high standing and operating for many years, secured by the state for the purposes of this case.

The Commission saw and heard the witnesses, painstakingly examined their testimony and with the discretion allowed it under the law, arrived at what it determined the fair and reasonable value of plaintiff's property. And while it is the duty of this court to make an independent investigation of the facts which it has done, this court should be careful not to substitute its judgment for that of the Commission, unless it is clear that the Commission erred.

The effect of the opinion and findings of the majority, if adopted on sufficient of the items, makes a rate base from which it may be argued that the rate allowed the plaintiff is confiscatory. The evidence in my opinion fails to disclose on such items sufficient reasons for setting aside the findings of the commission and substituting those of this court, nor does the evidence justify a finding of this court that a gate rate of 40 cents to the distributing companies is fair and reasonable.

The important questions will be discussed in their order.

Used and Useful Gas Acreage

The company owns 1,262,361 acres of gas rights. The Commission found that 71,267 of such leases were used and useful and devoted to a public use, and valued such acreage at $2,880,390. (Book value.)

Officers of the company testified that they considered all of the 1,262,361 acres of gas rights owned by the com-

pany as necessary and a prudent purchase. The majority opinion holds that the public service commission may not substitute its judgment for that of the officers of the companies. True ordinarily, but the rule also is that "what [fol. 383] the company is entitled to demand in order that it may have just compensation, is a fair return upon the reasonable value of the property at the time it is being used for the public." (Pon on Public Utilities, sec 591; San Diego Land & Town Co. v. National City, 174 U. S. 739; 43 L. Ed. 1154.)

The facts show clearly, in my opinion, that all of such gas rights are not now used, and that the present consumers do not and will not in the near future receive any benefit from them.

These investments in gas reserves, by the plaintiff, perhaps were prudent, but they should not be used as a base on which to estimate the rate for present consumers. None but the 71,267 acres of leases allowed by the commission are in my opinion used and useful and devoted to the public use.

This 71,267 acres comprises 50,000 acres proven in the Amarillo field with all the wells in that field, and 21,261 acres, all the developed, proven and probable acreage in Kansas, Oklahoma (except Hugoton); with all the wells in those fields the recoverable gas reserve in this 71,267 acres is sufficient to furnish all of the company's requirements, excluding the gas purchased under its purchase contracts, on the basis of its requirements for the year 1930, for twenty-two years.

The acreage in the Hugoton field excluded comprises 123,440 acres. None of the company's acreage in this field is drilled, and all of it is distant at least ninety miles from any pipe line owned by the company. It is held by the company through ten-year leases with about seven years yet to run. These leases require an annual rental be paid and that a well be drilled within the term of the lease. The number of these leases is in excess of 500. The cost of drilling and equipping a well in this field is not less than $20,000, and if the company is to hold these leases it must drill within the next seven years over 500 wells at a cost of over $10,000,000 and in addition pay annual rental in a substantial amount.

[fol. 384] The prospective acreage excluded by the commission amounts to 998,287 acres; it is "wildcat" terri-

tory. Its value is for oil rather than gas. It is scattered. Very little of it is available to the company's pipe line.

In the assignment of 71,267 acres of leases as used and useful, there are 27,910 acres of land in the Sweet proven area of the Amarillo field, which are not developed, and 1,385 acres in Kansas and Oklahoma, 325 acres of which are proven and 1,060 acres probable, which are yet to be drilled, with sufficient reserves of recoverable gas to last for twenty two years. In addition to this reserve, the company owns purchase contracts entitling it to the gas of 782,421 acres in Kansas and Oklahoma, having 1,502 wells and a daily open flow of 2,138,170 M. C. F.

Gas consumers should not be required to pay a rate for gas based on a return on the valuation of leases which are not used for them, and which if ever used will not be until the distant future.

The gas situation, in this territory, has undergone a complete change within the last five years. The Amarillo and Hugoton fields have been developed within that time. Prior to that time the problem was how and where to get gas. Now the problem is to find a market. Utilities then based their rates on the presumption that the gas supply would be exhausted in from seven to ten years. Now the supply appears almost inexhaustible.

Doctor Moore, state geologist of Kansas, testified that the recoverable gas in the Hugoton field alone is sufficient to supply all of the requirements of Kansas, domestic and industrial, at the present rate of consumption, for over one hundred years.

It is a matter of common knowledge that there was recently brought in the "Burton" field within three miles of this company's pipe line, with undefined limits, having wells with an open flow of 270,000,000 cubic feet per day, with a rock pressure of 1,200 pounds.

Another matter having a bearing on this controversy is [fol. 385] the problem confronting the Texas railroad commission in the Amarillo field as to means of providing a market for the vast amount of "shut in gas"; that is, gas wells which have been drilled by independent operators which are shut in for lack of market.

The first attempt to provide a market for this shut in gas was by the common-purchaser act, which required purchase of this gas by the gas companies. That act was de-

clared unconstitutional, whereupon the Texas commission recently made an order limiting the "take" to 4 per cent of the potential (open flow). The object of this order appears to be two fold, first to conserve the gas in the sweet proven area in the Amarillo field for domestic and industrial uses; second, to provide a market for this shut in gas and a ratable taking from all wells. This order is in litigation. Whether or not it may be sustained makes little difference to this plaintiff. It may purchase gas from the shut in wells, many of which are within two miles of its line, or it may develop its own acreage (50,000 acres) by drilling additional wells.

That is to say, the effect of the Texas order, if sustained, is not to require the company to have additional acreage, but to require additional wells on the acreage which has been allotted to it; or the company if it prefers, can dispense with its reserves and in lieu thereof purchase some of the vast quantity of gas available from the "shut in wells," which under present conditions can find no market.

The action of the Kansas Commission in including in the rate base only that acreage which presently and will in the near future be used and useful is well supported by the authorities. (See United Fuel Gas Company v. Public Service Commission, 73 Law E. [U. S.] P. 402, 78 U. S. P. 322; United Fuel & Gas Co. v. Public Service Commission of West Virginia, 178 U. S. 722, 73 Law Ed. [U. S.] 402; City of Erie v. Public Service Commission, 278 P. A. 512; 123 Atl. P. U. R. 1924 D. 89; Logan Gas Company v. Public [fol. 386] Utilities Commission of Ohio, 189 N. E. 575; Columbus Gas and Fuel Company, No. 5925, supra.)

In my opinion the Commission was well within its powers in finding that 71,267 acres of plaintiffs' gas reserves, which are in addition to its purchase contracts, covering 782,421 acres and 1,502 wells, with a potential of 1,532,625 M. C. F. per day, are used and useful to the company's developed acreage 27,910 acres of which is in the sweet proven gas area of the Amarillo field. The testimony of the officers of the company that they considered all of the 1,262,261 acres held by it as necessary for its future requirements, is not sufficient to overcome the actual facts, that it has an adequate supply for twenty-two years in the future. It would be contrary to common sense and justice to require the present consumers to pay for gas reserves which are not now used and which might never be used for their needs.

The facts and circumstances disclosed by the record in this case present a problem different from the ordinary rate case. We have here a producing gas pipe line built for the purpose of supplying already existing customers. Result:—going-concern value is very largely opinion based upon theory, when the theory is not supported by the facts.

Mr. Black, testifying for the Commission, found the going value to be $3,820,000. Mr. Hamilton, engineer for the Doherty Corporations, found it to be 8,898,532. The Commission found $2,000,000 as a sufficient allowance for this element of value. Mr. Hamilton testified: "I just took 10 per cent of the physical property value for this particular case for that item."

"Q. You have not itemized it?

"A. No, I have not itemized it in any way.

"Q. As I understand, then you did not arrive at it by finding the cost of attaching this business.

[fol. 387] "A. It is partially the cost of attaching the business, and the time of the engineers and others in negotiating the contracts, but that, for a wholesale situation, is a small item. The largest cost is the excess capacity that you will have for a period of three years, while your distributing companies are getting up to a point where they use the amount of gas that the size of the system is predicated on."

It is apparent from the record that Mr. Hamilton and Mr. Black considered the "idle plant" while the line was reaching the maximum capacity as the largest element of cost to be considered in going-concern value.

Both witnesses testified that the going-concern value for a pipe-line company would be less than the going value for a distributing plant. Mr. Hamilton testified to the difference between going value for a distributing plant and a pipe-line company as follows:

"Q. Do you mean to say, Mr. Hamilton, that every plant of the same value should have the same allowance for going value?

"A. No, because there would be a different allowance between your pipe-line plant or your distribution plant or an electric plant or something like that. There might be a wholly different basis.

"Q. For instance you take the distribution plant, take the one here in Topeka, for example——

"A. Yes, sir.

"Q. If you assumed that you would reproduce it now, and it had no customers, it would mean you would have to attach in that case, thousands of customers before the business was established?

"A. That is true, and 10 per cent allowance in that distribution plant would not be sufficient in my judgment.

"Q. Then take a pipe-line company like this, and the number of customers you have is not very large, very many involved, don't exceed three or four hundred?

"A. That is true.

"Q. That should be taken into consideration in arriving at the going value in this case?

"A. That is true."

It is perfectly apparent that both witnesses arrived at their calculations for idle plant upon a hypothetical basis without considering the actual facts and experiences of the company. It appears that the Commission applied the tests [fol. 388] which both engineers laid down as a proper measure of determining going-concern value and found that $2,000,000 was a sufficient and proper allowance.

The record shows clearly that on the major part of the pipe-line system there was very little idle plant following the construction period.

Many reasons may be advanced as to why a going-concern value should be added to the physical value of the property of the distributing companies which does not obtain as to the production and transmission system. This line was built for the definite purpose of supplying customers already secured and there appears little or no justification for adding a large going-concern value to it.

It is doubtful if a going-concern value amounting to millions of dollars can be established on a theory that expenses are to be incurred after the property has been reproduced when as a matter of fact such expenses were not incurred. How can it be said that there would be any expense of attaching business to a producing pipe-line company which has been built for the sole purpose of supplying already existing customers?

The argument that the cost incident to training personnel is a proper basis of going-concern value in this case is not

good, because the business of producing, transporting and distributing gas has been so long in operation that an abundant supply of well-trained personnel is always at the command of the company. In these times there is probably a considerable oversupply. See (in re appeal Columbus Gas and Fuel Co., [Ohio], No. 5935.)

The Commission, in my opinion, was right when it gave consideration to the cost of organizing the operating company, organization legal expenses, cost of records, and some interest and depreciation on idle plant, taking into consideration that there has been very little, if any, idle plant in the system.

It may be observed in passing that the interest charged [fol. 389] on the books of the company to the cost of Wichita Ottawa 20 inch line amounted to $24,444.04, while Mr. Black allowed for interest on this same line $198,544, and Mr. Hamilton allowed $320,182, indicating that both engineers were not only liberal, but, in fact, made excessive allowances for interest compared with the actual experience of the company. Under all the circumstances the allowance of $2,000,000 made by the commission was reasonable and adequate.

Rate of Return

In considering what is a fair rate of return to be earned by the pipe line company in connection with the reasonableness of the gate rate contract of 40 cents, we must take into consideration what it must earn in the light of its situation, its requirements and its opportunities. In dealing with its affiliated distributing companies we should consider the fact that the company should be allowed to earn on the value of its property employed in serving the public with its pipe line an amount equal to that generally being made by the same business undertakings which are attached by the same risks and uncertainties. It should also be allowed to earn an amount reasonably sufficient to assure confidence in its financial ability.

There was testimony for the plaintiff that an 8 per cent return is usual. Other testimony placed the rate at from 6 to 8 per cent. Practically all of the witnesses agreed that some consideration should be given to the fact that this company was not an ordinary public utility company, but one of a large system organized for the purpose of main-

taining the credit of the constituent companies and securing financial assistance.

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It is apparent from the affiliation and mutual assistance rendered by the great and efficient Doherty organization that this particular plaintiff is and has been able to sell its securities at an "interest rate that was from a half to three fourths per cent less than anything else that was put out [fol. 390] at about that time on a similar project, and that if gets better terms on its mortgages. Because of this situation it was able to sell its 5½ per cent bonds for 96¼. This plaintiff having ample resources does not necessarily have to issue securities now or six months from now or two years from now. "It picks and chooses its time when the markets are right."

The record shows this plaintiff sold twelve million dollars of first mortgage, pipe line 6 per cent gold bonds at par. It is apparent therefore that it is able to obtain funds at a very low rate and is assured of financial stability and a supported credit which enables it to raise all necessary money for the proper discharge of its duties at a low rate of interest. It is apparent also that there is little risk or hazard in its business. The pipe line system which it has established is a permanent fixture for an indefinite period. It has a gas reserve which insures it of a supply of gas lasting well into the future. The territory which it serves is well protected; it has almost a monopoly on the territory which it serves due to the fact that the distributing units are affiliated companies and it would be economically unsound for another pipe line company to invade its territory.

We are also confronted with changed conditions affecting opportunities for investments which tend to limit the amount of the return. Annual returns upon capital have materially decreased in the past two or three years. Businesses generally are satisfied with a very low rate of return. All businesses, including that of public utilities, are satisfied with a much less rate of return than they were three or four years ago when annual returns upon the capital were unreasonably high.

The Cities Service Gas Company is not an ordinary public utility. It is one of a large system organized for the purpose of maintaining the credit of subsidiary companies and

assisting them in their finances. It has been able to extend its business so as to meet increased demands, to pay its [fol. 391] operating expenses, including interest on money borrowed, to pay dividends of 8 per cent upon its capital stock and accumulate a large surplus. (See Smith v. Illinois Bell Telephone Co., 282 U. S. 159, 161.)

It is apparent from the record that the operations of this plaintiff have been highly successful and enormously profitable. It was organized in 1926, acquiring the assets and assuming liabilities of the following companies: Empire Natural Gas Company, Empire Gas and Pipe Line Company, Kansas Oklahoma Gas Company, Empire Gas and Fuel Company (gas properties only).

At that time the plant investment of these companies, including uncompleted job orders, was $52,182,525.98. Reserves for depreciation and depletion had been accumulated out of earnings in the amount of $22,423,936.95, or 42.97 per cent of the plant investment. They had accumulated a surplus amounting to $14,903,660.21, equal to 87.26 per cent of the total capital stock of the companies taken over.

The combined reserves for depreciation and depletion and surplus amounted to $37,327,527.16, equal to 218.55 per cent of all outstanding capital stock of the companies and 71.53 per cent of the plant investment. They were able to loan other affiliated companies $7,559,571 in addition to paying bond interest and dividends.

When this plaintiff was organized and its books opened, 17,080,000 of capital stock and $2,000,000 of bonds became immediately $25,000,000 of common stock and $25,000,000 of 5½ per cent bonds; its reserves for depreciation and depletion became $7,760,706 instead of $22,423,939, as they were before the consolidation. No surplus was carried over into the new corporation.

A glance at the financial history of the company since the consolidation in 1926, is of more than passing interest. This history shows that surplus has been accumulated in excess of all interest and dividends paid of $9,044,629 to June 30, 1931; its depreciation and depletion reserves have [fol. 392] been increased to $10,818,020. Its total assets have increased from $60,595,001 as of December, 1926, to $109,431,039 as of June 30, 1931. This increase was accomplished with the addition of the outstanding stock and bonds

of only $28,305,700 and loans of $9,000,000. The company has been able to advance to affiliated companies $2,677,131. During all this time it paid interest on its bonds and dividends on its capital stock; in 1928, $1,000,000 dividends, and in 1929 and 1930, $2,000,000 each on dividends, which is at the rate of 8 per cent per annum. Its earnings before interest were as follows:

1927	$5,335,739	1930	$3,829,480
1928	$6,053,621	Twelve months ending	
1929	$8,060,793	June 30, 1931	$3,741,966

Its net profit after paying all interest and other charges providing for substantial allowances for depreciation and depletion amounted to the following percentages of its outstanding capital stock during each of the years 1927 to 1930, inclusive:

1927	9.96%	1929	14.53%
1928	6.75%	1930	10.82%

The plant investment, including uncompleted job orders, increased from $54,243,128, December 31, 1926, to $99,003,998, June 30, 1931, an increase of $45,760,872. A considerable program of expansion was carried out, a large line was constructed from Amarillo to Wichita; a line was extended from near Hutchinson north into Nebraska; lines were extended into Missouri; such construction involved large expenditures which affected the operating expenses of the company.

It is a matter of common knowledge that price levels were higher. The purchasing power of the dollar was very much less than now, 8 per cent was considered a fair and reasonable rate of return.

Under the present low level of prices the purchasing power of a return of 6 per cent is greater than the purchasing power of a return of 8 per cent was during the periods of higher price levels.

[fol. 393] A return of 6 per cent is not unreasonable at this time. In fact, the great majority of concerns now doing business are glad to earn as much as 6 per cent, and are fortunate to do so. Even a 5 per cent return at this time would not be confiscatory.

I am of the opinion that in view of the financial history of this plaintiff its highly profitable experience, the fact that it is a part of a large system with its market assured through affiliated distributing companies, its large gas reserves, and all attending circumstances, a return of 6 to 8 per cent is reasonable and 5 per cent would not be confiscatory.

United Railways & Electric Co. v. West, 280 U. S. 234-291, 74 L. Ed. 390, is cited and relied on in the majority opinion as sustaining the conclusion that the rate of return must be 8 per cent. The court in the West case held that under the circumstances of that case a rate of 6.26 per cent was insufficient. Three members of the court dissented. In my opinion the decision in the West case does not sustain the majority opinion in this case. It was among other things said in the syllabus:

"* * * The fair rate of return to which a public utility is entitled is to be tested primarily by present-day conditions, and not by what may have been a proper rate in the past. * * * In determining whether the rates established by a public service commission are so inadequate as to be confiscatory, the court must determine what will constitute a fair return, to the best of its ability, in the exercise of a fair, enlightened, and independent judgment as to both law and facts. * * * A rate producing a return of 6.26 per cent on the valuation of the property of a street railway company will be considered so inadequate as to amount to a taking of its property without due process, where it is shown that while the total number of passengers carried has for some time steadily decreased, the number carried during rush hours has increased, resulting in an increase of expenses in proportion to the whole number of passengers carried and that, in borrowing money with which to finance its operations, the company has been obliged to pay a rate of interest ranging well over 7 per cent."

[fol. 394] In the opinion it was said (p. 250):

"A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same gen-

eral part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. A rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market and business conditions generally. * * * Investors take into account the result of past operations, especially in recent years, when determining the terms upon which they will invest in such an undertaking. Low, uncertain or irregular income makes for low prices for the securities of the utility and higher rates of interest to be demanded by investors. The fact that the company may not insist as a matter of constitutional right that past losses be made up by rates to be applied in the present and future tends to weaken credit, and the fact that the utility is protected against being compelled (p. 251) to serve for confiscatory rates tends to support it. In this case the record shows that the rate of return has been low through a long period up to the time of the inquiry by the Commission here involved."

On page 251 appears the following:

"Since 1920 the company has borrowed from time to time some $18,000,000 upon which it has been obliged to pay an average rate of interest ranging well over 7 per cent and this has been, upon the valuation fixed, with an allowance for depreciation calculated with reference to that valuation, and upon the then prescribed rates, the company for the years 1920 to 1926, both inclusive, obtained a return of little more than 5 per cent per annum."

On page 252 appears the following:

"In this view of the matter, a return of 6.25 per cent is clearly inadequate. In the light of the recent decisions of this court and other federal decisions, it is not certain that rates securing a return of 7½ per cent or even 8 per cent on the value of the property would not be necessary to avoid confiscation. But this we need not decide, since the company itself sought from the commission a rate which

it appears would produce a return of about 7.44 per cent, at the same time insisting that such return fall short of being adequate.

[fol. 395] On page 249 appears the following:

"What is a fair return within this principle cannot be settled by invoking decisions of this court made years ago based upon conditions radically different from those which prevail today. The problem is one to be tested primarily by present day conditions. Annual returns upon capital and enterprise, like wages of employees, cost of maintenance and related expenses, have materially increased the country over. This is common knowledge. A rate of return upon capital invested in street railway lines and other public utilities which might have been proper a few years ago no longer furnishes a safe criterion either for the present or the future."

The court was there considering a rate for a street railway. It is a matter of common knowledge to which we may not shut our eyes, that bus transportation and the use of private automobiles the country over have cut deeply into the revenues of street railway companies. The very opposite condition exists in connection with the plaintiff which has made big returns, paid its interest and dividends, accumulated a surplus, loaned money, and is able to float its securities at will and on better terms than other like utilities. A gas pipe-line company which practically has a monopoly in its field.

Applying to the instant case the principles stated by Mr. Justice Southerland in United Railways v. West, supra: Considering all the facts shown by the record and attending circumstances, it must appear beyond question that a rate of return to the plaintiff of from 6 to 8 per cent on the value of its property used and useful in its business would be a fair return when protected by the state—even a rate of 5 per cent in these times would not be confiscatory.

In Wabash Valley Electric Co. v. Ralph M. Young et al., No. 112, a case in which a decision was handed down January 9, 1933, in an opinion by Mr. Justice Southerland it was said:

"It is true, as appellant point out, that in United Railways v. West, 280 U. S. 234, 251-252, this court held that a rate of return for a street railway of less than 7.44 per cent was confiscatory, saying that sound business manage- [fol. 326] ment required that after paying all expenses of operation, etc., 'there should still remain something to be passed to the surplus account,' and that a rate of return which did not admit of that being done was not sufficient to enable a utility to maintain its credit and raise money for the proper discharge of its public duties. Many cases were cited tending to show that a return of 7½ per cent, or even 8 per cent, might be necessary, but it was said (pp. 249-250) that no rule could be laid down which would apply uniformly to all sorts of utilities. 'What may be a fair return for one may be inadequate for another, depending upon circumstances, locality and risk.' A street railway company, compelled to meet the growing competition of private automobiles, public omnibuses, and other motor carriers, well might sustain such losses of revenue because of the decreased number of passengers carried, as to require a larger rate of return than would be required by an electric company like appellant, which not only enjoys a practical monopoly in the field where its services are rendered, but whose financial structure, it fairly may be assumed, is greatly strengthened by its affiliations and by the interested support of the parent company to which it belongs. On the whole we are unable to conclude that a 7 per cent rate of return, under the facts here disclosed, is so low as to be confiscatory. See Smith v. Illinois Bell Tel. Co., supra, at pp. 160-161."

In Kankakee Water Co. v. Gilbert, decided by the United States district court for the eastern district of Illinois January 6, 1933, it was said that "under existing depressed, industrial and financial conditions a rate of 5.17 per cent was not confiscatory." The court said:

"Under the existing generally depressed industrial and financial conditions, indicating a greatly abnormal condition both generally and locally, all of which appears in the record, we are not warranted in finding that the probable return of 5.17 per cent upon the valuation as aforesaid, furnished by the commission's prescribed rates, is con-

fiscatory. In this connection, we have considered the evidence of present return in industrial enterprises of other character, and that of similar utility companies, as well as the fact that plaintiff makes no claim and furnishes no evidence that new capital is at present needed in its business."

[fol. 397] The Henry L. Doherty Contract

The distributing companies pay to Henry L. Doherty 1¾ per cent of their gross revenue, an engineering fee equal to 5 per cent of construction, and in addition expenses, disbursements and per diem for Henry L. Doherty & Company representatives while at the property of the distributing companies or traveling for them on special matters.

The distributing companies also pay to the Gas Service Company for the same type of service. The commission allowed payment for the services to the Gas Service Company, but refused approval or payment to the Henry L. Doherty & Company on the ground that it was a duplication.

What happens is perfectly clear. The distributing companies have similar contracts with two of these other Doherty units for the same class or type of service—one with Henry L. Doherty, the other with the Gas Service Company. The latter furnished the services, the former did not.

The Public Service Commission made an allowance for the services by the Gas Service Co., but denied any allowance to Henry L. Doherty & Co. The majority opinion, while denying payment to Henry L. Doherty & Company because of failure of proof that services were rendered, holds that the contract is proper. With this I cannot agree.

Application of the rule that a public utility is entitled to charge such rates as will create a sufficient income to provide a fair return upon the value of its property used and useful and devoted to the public, does not authorize the owners of a utility to pay themselves increased operating expenses or to provide themselves with unconscionable profit because of their position. Funds for operating expenses are received from the public and to thus duplicate payments for services is unwarranted under any reasonable hypothesis.

[fol. 398] The record shows that the activities of Henry L. Doherty and Company embrace many matters which, by the greatest stretch of the imagination, could not be a proper operating charge to the distributing companies. These activities are largely devoted to the purchase and sale of Cities Service securities. Investments of the Cities Service Company and Henry L. Doherty & Company in oil development and others in no way results in a benefit to the distributing companies. It appears that no securities of the disfributing companies have been marketed by Henry L. Doherty and Company, and should there be, a separate fee would be charged for such services. The production, sale and transportation of oil and the handling of New York real estate are activities unrelated to the distributing companies and the consumers of natural gas have no interest in Mr. Doherty's oil or stock business and should not be compelled to pay the expense of transacting such business. There is no apparent reason why the patrons of these distributing companies should pay to help maintain an office in London. Yet for a period of years the distributing companies have been paying Henry L. Doherty & Company 1¾ per cent of their gross revenue from funds received from their patrons.

A number of companies are operated by Henry L. Doherty & Company at 60 Wall Street, which in no way, so far as the record discloses, contribute to the defraying of the expense of the operation of Henry L. Doherty & Company.

For example: The Gas Securities Company owned by Henry L. Doherty & Company, with offices at 60 Wall Street, with net assets of $23,252,907 and net earnings for 1929 amounting to $1,960,376, was not shown to have paid any revenue to Henry L. Doherty & Company.

The Gas and Electric Securities Company owned and operated by Henry L. Doherty & Company, with offices at [fol. 399] 60 Wall Street, has assets of $24,952,188, with an income of $2,086,069 in 1929, with no showing of revenue to Henry L. Doherty & Company.

This Henry L. Doherty contract apparently is for the purpose of keeping Henry L. Doherty informed as to the activities of the distributing companies and the protection of his investment rather than for the benefit of the distributing and pipe-line companies. Except to the extent

that any specific services may be rendered, there is nothing in the record to show any benefits to the distributing companies from his contract. The benefit is largely for the sole benefit of Mr. Doherty's holding company, The Cities Service Company.

The activities of Henry L. Doherty & Company may well be considered a burden to the distributing and pipe-line companies, rather than a benefit. First, because they must immediately transfer all their earnings to Henry L. Doherty & Company, leaving them dependent upon it for financial existence for which they must pay, while Henry L. Doherty & Company has the advantage of these earnings and the use of the funds of the underlying companies pending their distribution as dividends; and second, because they must pay Henry L. Doherty & Company 5 per cent of the cost of their construction projects, regardless of the benefit received or the services performed. While this cannot enter into the expense in determining a rate to be charged the consumer, it does affect the financial stability of the distributing and pipe-line companies.

Not only did the parties fail to produce any evidence to sustain their rights to such fee, as stated in the majority opinion, but they failed in my opinion to justify the need of such a contract.

Interest During Construction

Black and Hamilton both calculated interest during construction for the same period. Black allowed a rate of 6 per cent, Hamilton 8 per cent. The question is, what is a proper rate?

The plaintiff argues that "if 8 per cent is a proper rate of [fol. 400] return for the investor to receive after the project is placed in operation, on what theory or by what process of reasoning can the conclusion be reached that this same investor is entitled to less return on his money during the period the plant is being constructed? You have the same investor and the same money going into the same project. Whatever is fair in one case must be fair in the other."

With this contention I do not agree. There is little relation to be found between a rate of interest to be allowed for the use of money borrowed or advanced in construction

and a rate of return on the value of property when subsequently put into public service. The latter involves the contingencies of operation and many other considerations.

Interest during construction may be a different rate. It is a fixed allowance and the hazards which may accompany the earning of a rate after the business is in operation are not present.

The allowance by Black as heretofore said was not only adequate, but excessive. Hamilton's allowance was entirely out of line with the actual facts.

On September 1, 1931, there were properties of the City Service Gas Co. used and useful in the public service, as follows:

	Number and title of account	Reproduction cost less depreciation
1307	Production—rights of way	$55,982
1310	Production—field measuring, station structures	35,909
1311	Production other structures	47,876
1312	Production gas-well construction	1,294,710
1313	Production gas-well equipment	658,439
1314	Production field-line equipment	3,126,159
1315	Production field measuring station equipment	265,746
1316	Production drilling and cleaning equipment	27,908
1317	Production other equipment	1,333
1325	Transmission land	145,202
1327	Transmission rights of way	1,657,530
1328	Transmission compressing station structures	1,466,102
1329	Transmission measuring station structures	133,310
1330	Transmission other structures	113,341
1331	Transmission compressing station equipment	8,048,910
1332	Transmission measuring station equipment	759,625
1333	Transmission line equipment	39,432,331
1334	Transmission other equipment	5,633
[fol. 401]		
1376	General other land	3,655
1379	General other structures	94,687

Number and title of account	Reproduction cost less depreciation
1380 General office equipment	106,035
1381 General store equipment	1,805
1382 General shop equipment	23,084
1384 General stable equipment	568
1384 General garage equipment	81,448
1385 General laboratory equipment	8,202
1386 General telephone and telegraph system	415,070
1387 General tools and implements	44,070
1388 General other equipment	21,832
	$58,077,111
Preliminary organization expense	$480,008
Engineering and superintendence during construction	2,881,000
Administration and legal expense during construction	304,084
Taxes during construction	875,171
Interest during construction	3,883,282
Miscellaneous construction expenditures	608,169
Cost of financing	
Working capital	775,000
Materials and supplies	628,675
Going-concern value	2,000,000
Gas in lines	22,000
Gas leases	2,874,390
Rate base	$73,409,190

The following observations may be made with reference to the above accounts: In accounts number 1307 and 1327 the commission arrived at the price of $1.47 per rod by taking actual acreage cost on 31 per cent of right of way and damage cost shown in the record as being $1.08 plus the agreed 10 cents per rod for expense of abstracting and recording, plus 22 cents per rod for expense of acquisition, plus 7 cents per rod for engineering, which is at the rate of 5 per cent. There is nothing in the record contrary to the above that warrants the setting aside of the findings of the commission.

Regarding account 1312, it seems to me that the sum of $57,235 deducted by the commission on the legal theory then

advanced is not tenable and that said sum should be restored. Likewise the item of $84,318 should be restored since the engineer for the commission for reasons appearing in the evidence omitted certain items in his calculations which properly belonged therein. I therefore have con- [fol. 402] cluded and found that value of account 1312 should be fixed at $1,294,710.

In relation to account 1314, it might appear that engineer Black's figure is an estimate based upon an arbitrary figure of 50 per cent of the depth of main lines for pipe lines and that Eastman, who testified for the company, was giving evidence from actual size, but a close examination discloses that Eastman's unit prices which he was applying to field lines were not in accordance with the actual depth as shown by inspection, but that with the exception of field ditches excavated by trench machines he applied to his calculations of quantities the width and depth of ditches set forth in exhibit 73, as an average of all underground field pipe lines. I find nothing in the record to warrant setting aside the finding of the commission on this account number 1314.

Considering accounts 1325 and 1328 and 1331, which among other properties, dealt with the Hog Shooter property, station and equipment, account 1325, being as to land owned in fee except general land, account 1328 relates to station structures, and account 1331 relates to station equipment. In this connection it may be said that the argument advanced that between February, 1931, when the company for taxing purposes returned the Hog Shooter property as abandoned, and July, 1931, when the commission ordered the hearing, that the discovery of new gas fields made the Hog Shooter station available, although still not in use during the hearing, does not favorably impress me and I therefore conclude that $2,000 should have been deducted for the Hog Shooter property in account 1325, making the account valuation $145,202 and that $49,560 should have been deducted for Hog Shooter station structure in account number 1328, making the account valuation $1,466,102, and that in account 1331, the Hog Shooter equipment in the amount [fol. 403] of $414,925 should have been deducted, making the account valuation $8,048,910.

Considering account 1333, the per cent condition of the property found to be 90.1 per cent by the commission and the cost of rock excavation as found by the commission and

approved by the majority opinion and in that I concur, leaving only the quantities of rock excavated to be considered and at the threshold of that consideration permit me to state that I agree with the majority that the overcuts should be excluded. In connection with quantities of rock excavated, it should be noted that since the hearing by the commission and before the trial by this court certain inspections were made on one line and the result of such inspection was introduced in evidence at the trial herein. But an examination of that evidence so introduced discloses nothing that will warrant this court in disturbing the finding of the commission in account number 1333, to wit, $39,432,331.

Considering other valuations I have discussed fully gas leases valued at $2,874,390 and the going concern value fixed at $2,000,000.

I concur with the majority that cost of financing should not be included in the rate base.

There remains, therefore, only the following items, to wit: preliminary and organization expense, engineering and superintendence during construction, administration and legal expense during construction, miscellaneous construction expenditures, taxes during construction and interest during construction.

Elsewhere in this opinion I have approved the principle of averaging the values as well as the earnings during the test period, but it should be noted that the valuations set out in the opinion are not average values. They are values of September 1, 1931. Using the valuation found as of that date, to wit, $73,409,190, I find that the plaintiff has failed to show that the 30-cent rate fixed by the commission is confiscatory.

[fol. 404] Under the 40-cent rate the Cities Service Gas Company is earning 8.96 per cent a year upon the present value of its properties.

I find that on the valuation of $73,409,190 and at a rate of 30 cents the return would be 6.41 per cent. If averaged over a period for the calendar year 1930 and the year from June 30, 1930, to June 30, 1931, and the year from June 30, 1931, to June 30, 1932, the return at 30 cents would be 6.849 per cent.

The record shows that by far the largest part of the product handled by the plaintiff in this territory is "industrial gas" which is sold to individual consumers at an average of about 15 cents per M. C. F. A little more than one-third of the city gate rate to the distributing companies 40 cents. Part of this product actually sold to "industrial consumers," and part to "domestic consumers." The industrial consumer (ordinarily) is one who uses a continuous supply of the product through the twenty-four hour period, thereby taking the "off peak" load. The domestic consumer is the housewife, office or mercantile establishment which (ordinarily) uses the supply during the day but not at night.

The rule is that the price for gas should never be unnecessarily low to some consumers while high to others. It should always be high enough to avoid loss to the utility. Special rates for a large portion of the company's output can be justified only upon the ground that they contribute to the public advantage. Discrimination in price based solely on amounts consumed by different patrons cannot be justified, and rebates to certain businesses only because they use a large amount of gas is discriminatory.

Unless the lower rate can be justified upon the ground that it contributes to the general public advantage, the company and not the consumer must bear the loss if one occurs through that class of business. Of course, a schedule of rates contrived for the purpose of selling gas in order that [fol. 405] industries using it may operate more economically than can be done with other fuels may, under some conditions, furnish sufficient grounds for a differential rate. It should be clear, however, that the rate named is not a losing one, and that it will increase the company's profits. (The burden of showing this is on the utility). Differentials of this kind afford no justification for a practice which seeks to charge a large consumer a low price and a small consumer a higher price merely because of a difference in size.

All such considerations should be included in the standard schedule in order that all customers, or possible customers having similar conditions, will receive service at similar rates. A company is not justified in transferring any considerable portion of the costs from one class of

patrons to another class. Schedules should be arranged so that as near as possible each patron will pay his fair share of the cost. No rate should be established unless it provides some profit—that is, some return over and above the costs of operation.

There can be no possible justification for the company to depart from its published schedule of prices, or to give any advantage, directly or indirectly, to one customer not offered to others enjoying or seeking the company's service under like conditions.

If the so called industrial business pays a sufficient profit to bear its part of the load, its part of the upkeep of the general investment, a lower rate is allowable, but, as I see it, the burden is upon the utility to show that such service is self sustaining. In case of loss the utility should not expect the domestic consumer to sustain the industrial consumer's part of the investment.

In the instant case, the increased use of industrial gas has not been manifest in any reduction to the domestic consumer. The plaintiff has insisted and still insists on the gate-rate charge of 40 cents—so that increased industrial business has not led to reductions.

[fol. 406] It appears to be a matter of common knowledge that the distributing companies contract, sell and deliver gas also to some domestic consumers at what appear to be discriminatory rates. They do this apparently on the theory that it is justified in meeting competition with other forms of fuel. This practice of furnishing gas to domestic consumers, such as large mercantile stores and hotels, at rates of from 10 to 17 cents per M. C. F., while charging other individual domestic consumers rates ranging from 75 cents to $1.50 per M. C. F., may amount to unlawful discrimination. This question has not been briefed and I express no opinion thereon. It is one which might well warrant the conclusion that the Doherty companies are not in court with clean hands, and for that additional reason their prayer for equitable relief should be denied. A utility procures its charter and operates through sufference of the state. Rates for its product are allowed and approved by the state's regulatory body. In this instance, the Public Service Commission allows and approves local rates to the consumers. The companies involved here having applied for and procured approval of such rates are bound thereby

and for them to follow the practice of disregarding the approved schedule of rates in favoring some consumers above others, is contrary to law. (See R. S. Kan. 66-107, 66-108, 66-109; Empire Natural Gas Co. v. Thorp, 121 Kan. 116; Kansas Electric Power Co. v. Thomas, 123 Kan. 321.) It should not be tolerated, much less have the approval of this court.

If it be argued that so-called industrial sales are not made at a loss, that there is an actual profit on sales to individual consumers at rates as low as from 10 to 15 cents per M. C. F., it certainly is unreasonable to hold that a rate of 30 cents at the city gates to the distributing companies is confiscatory. The distributing company represents all of the consumers collectively, and the argument that it can dispense gas to one of its patrons at from 10 to 15 cents [fol. 407] per M. C. F. at a profit and that a rate of 30 cents to it at the city gates for all its patrons collectively is confiscatory, does not appeal to my reason. The burden rests upon the utility to show clearly that the rate (30¢) is confiscatory. This it has failed to do.

Knoxville v. Water Co. (212 U. S. 1, at page 16), Mr. Justice Moody, speaking for the court, said:

"If a company of this kind chooses to decline to observe an ordinance of this nature and prefers rather to go into court with the claim that the ordinance is unconstitutional, it must be prepared to show to the satisfaction of the court that the ordinance would necessarily be so confiscatory in its effect as to violate the constitution of the United States. In Ex parte Young, 209 U. S. 123, the last word of caution by this court was said (p. 166): Finally it is objected that the necessary result of upholding this suit in the circuit court will be to draw to the lower federal courts a great flood of litigation of this character, where one federal judge would have it in his power to enjoin proceedings by state officials to enforce the legislative acts of the state, either by criminal or civil actions. To this it may be answered, in the first place, that no injunction ought to be granted unless in a case reasonably free from doubt. We think such rule is, and will be, followed by all the judges of the federal courts. The same thought, in effect, was expressed in San Diego Land & Town Company v. National City, 174 U. S. 739, 754; judicial interference should never occur unless the case presents, clearly and beyond all doubt, such a

flagrant attack upon the rights of property under the guise of regulations as to compel the court to say that the rates prescribed will necessarily have the effect to deny just compensation for private property taken for the public use?"

The parties to this litigation have asked that the case be considered on its merits and a final determination reached. On page 147 of its brief the plaintiff says "We believe it to be most desirable that this court should examine the facts, as well as the law and give to the people the benefit of its authoritative decision upon the real question at issue."

In accordance with this expressed desire, the writer of this opinion has made an investigation of the facts and the [fol. 408] law and is of the opinion that the plaintiff has failed to show that the orders in question, made by the Public Service Commission of Kansas, are unlawful or confiscatory. In accordance with the desire of the parties, I have prepared and filed full findings of fact and conclusions of law in accordance with the views herein expressed. The bills should be dismissed.

[File endorsement omitted.]

[fol. 409] IN UNITED STATES DISTRICT COURT

SEPARATE FINDINGS OF HOPKINS, DISTRICT JUDGE—Filed Jan. 14, 1933

Findings of Fact

For a long period of years, more than twenty, Henry L. Doherty, doing business under the name of Henry L. Doherty & Company, has maintained a complete organization for the design, construction, operation and development of public utilities, and oil and natural gas properties. This organization is composed of experienced executives, financial advisors, construction, valuation, electrical, oil and gas engineers, geologists, chemists, technicians, experts, accountants, operators and lawyers. There are approximately 1,667 employees. In this organization Mr. Doherty maintains departments for the purchase, sale, promotion and transfer of

stocks of his various corporations, a foreign oil department; marine and tank car department; and oil production and refining department; a real estate division chiefly concerned with New York real estate, and maintains a London office.

II

The parties to this litigation are all units or corporations of the Doherty organization, and all have to do in some degree with the production, transportation and sale of natural gas to consumers of Kansas.

III

On July 2, 1931, an order was entered by the Public Service Commission of Kansas, on its own initiative, directed to the plaintiffs herein, except the Cities Service Gas Company, finding that the reasonableness of all contracts with, and charges made to, the respondents by corporations owning the stock of the plaintiffs, and of the contracts between Henry L. Doherty & Co. and respondents should be inquired into; the respondent distributing companies were ordered to show cause why payments made under such contracts, [fol. 410] if found to be unreasonable, should not be disallowed as operating expenses. A copy of said order is Exhibit A attached to the bills of complaint of the distributing companies.

IV

Pursuant to such order, extensive hearings were held. The properties of the Cities Service Gas Company, situated in five states were appraised by engineers for both parties and valued by the Commission. Findings and conclusions were filed by the Commission.

A petition for rehearing was filed, allowed, rehearing had, and the orders entered which are now submitted for review to this court.

V

The citizenship and official position of the parties are as stated in the bills of complaint. There is diversity of citizenship, a substantial federal question in each of the cases and more than $3,000 in controversy.

VI

The plaintiff distributing companies were engaged in the sale and distribution of natural gas to domestic and industrial consumers of 128 cities and towns in Kansas, procuring their gas from another of the Doherty units the Cities Service Gas Company. The Cities Service Gas Company, through Henry L. Doherty, has a practical monopoly on the sale of gas to the distributing companies. The arrangement being that the pipe line company will supply the present needs of the distributing companies at 40 cents per thousand cubic feet, delivered to their mains. This 40 cent rate is a private contract between the affiliated Doherty corporations.

VII

Except for qualifying shares, the common stock of the distributing companies is owned by the Gas Service Company, the stock of which in turn is owned by the Cities Service Company. The common stock of the Cities Service Gas Company [fol. 411] is owned by the Empire Gas & Fuel Company, the voting stock of which in turn is owned by the Cities Service Company. The Empire Gas & Fuel Company has a preferred stock issue outstanding in the hands of the public. Henry L. Doherty owns 35 per cent of the voting stock of the Cities Service Company. The Cities Service Company, by stock ownership, legally controls the policies of the distributing companies and the pipe line company; and Henry L. Doherty in fact controls the policies of all the corporations, including the Cities Service Gas Company. The distributing companies do not deal at arm's length with either the Cities Service Gas Company or Henry L. Doherty.

VIII

The Cities Service Gas Company was organized in 1926. It took over the physical properties of five pipe-line companies, having a plant investment account at that time of $52,182,525.98. These pipe-line companies served many communities in Oklahoma, Kansas and Missouri. The companies taken over were integrated, so that the gas could be run from the mains of one system into that of another, and the supply thereby made more dependable and economical. Natural gas had long been used for lighting and cooking in most of these cities and towns.

There are extensive and prolific gas fields at Amarillo, Texas, and Hugoton, Kansas. It is a matter of common knowledge these fields are being enlarged and extended so that the supply is dependable for all uses, for a long period of time. The Cities Service Gas Company now has an adequate and dependable supply of gas, available at all times at the city gates. Mr. Doherty, through the Cities Service Company, acquired the distributing companies in order to meet keen competition.

IX

[fol. 412] The distributing companies, as units of the Doherty organization, have each entered into a contract with the Henry L. Doherty Company which provides for services as follows:

1. Personnel (i. e., experienced executives and operators).
2. Executive service.
3. General accounting service.
4. Statistical service.
5. Purchasing service.
6. Designing and construction engineering.
7. Financial service.
8. Securities department.
9. Valuation.
10. Tax departments.
11. New business department.
12. Technical and research department.

X

The Gas Service Co., another Doherty unit, with offices in Kansas City, Mo., has a contract with the distributing companies similar in many respects to the one above set out in finding number nine. It provides that it furnish services as follows:

1. Furnish all administrative and executive service.
2. Financial aid and advice.
3. Purchasing and warehousing.
4. Engineering and operating supervision.
5. All legal services.
6. All insurance purchasing.
7. All general accounting and reports.

8. Supervision and handling of all tax matters.
9. Handling of all pay rolls.
[fol. 413] 10. Making of all audits and auditing reports.
11. Make all governmental and regulatory commission reports.
12. Supervision of all new business operations.
13. Make all vouchers and disburse funds.
14. Supervise and direct all public relations work.
15. Do all general and policy advertising.
16. Make all valuations and rates and handle all matters pertaining to rate litigation, and routine matters with regulatory bodies.
17. Make and follow up all construction and financial budget.

The Commission found that the amounts paid by the distributing companies under this contract with the Gas Service Company were not unreasonable, but refused to approve payments on the contracts set out in finding nine, because of duplication.

XI

The activities of Henry L. Doherty & Company embrace many matters not covered by the 1¾ per cent contract, the expense of which is not a proper operating charge of the distributing companies. These activities are: The promotion, sale and transfer of securities of the Cities Service Company and its affiliates. No securities of the distributing companies have been marketed by Henry L. Doherty & Company, and if they are, the contract provides for a separate fee for such services. The production, sale and transportation of oil and the handling of New York real estate are unrelated activities. The record discloses no reason for these distributing companies maintaining a London office. The consumers of natural gas have no interest in Mr. Doherty's oil or stock business, and his private businesses ought not to be thrown together with the business of serving the public, the expenses of all hopelessly intermingled.

On September 1, 1931, there were properties of the City Service Gas Company used and useful in the public service, as follows:

[fol. 414]

Number and title of account	Reproduction cost less depreciation
1307 Production—rights of way	$55,982
1310 Production—field measuring station structures	35,909
1311 Production—other structures	47,876
1312 Production—gas-well construction	1,294,710
1313 Production—gas-well equipment	658,439
1314 Production—field-line equipment	3,126,159
1315 Production—field measuring station equipment	265,746
1316 Production—drilling and cleaning equipment	27,908
1317 Production—other equipment	1,333
1325 Transmission—land	145,202
1327 Transmission—rights of way	1,657,530
1328 Transmission—compressing station structures	1,466,102
1329 Transmission—measuring station structures	133,310
1330 Transmission—other structures	113,341
1331 Transmission—compressing station equipment	8,048,910
1332 Transmission—measuring station equipment	759,625
1333 Transmission—line equipment	39,432,331
1334 Transmission—other equipment	5,633
1376 General—other land	3,655
1379 General—other structures	94,687
1380 General—office equipment	106,035
1381 General—store equipment	1,805
1382 General—shop equipment	23,084
1383 General—stable equipment	568
1384 General—garage equipment	81,448
1385 General—laboratory equipment	8,202
1386 General—telephone and telegraph system	415,070
1387 General—tools and implements	44,979
1388 General—other equipment	21,832
	$58,077,111

Number and title of account	Reproduction cost less depreciation
Preliminary organization expense	480,008
Engineering and superintendence during construction	2,881,000
Administration and legal expense during construction	304,084
Taxes during construction	875,171
Interest during construction	3,883,282
Miscellaneous construction expenditures	608,169
Cost of financing	
Working capital	775,000
Materials and supplies	628,675
Going-concern value	2,000,000
Gas leases	2,874,390
Rate Base	$73,409,100

The following observations may be made with reference to the above accounts. In accounts number 1307 and 1327, the commission arrived at the price of $1.47 per rod by taking actual acreage cost on 31 per cent of right of way and damage cost shown in the record as being $1.08 plus agreed 10 cents per rod for expense of abstracting and recording, plus 22 cents per rod for expense of acquisition, plus 7 cents per rod for engineering, which is at the rate [fol. 415] of 5 per cent. There is nothing in the record contrary to the above that warrants the setting aside of the findings of the commission.

Regarding account 1312, it seems to me that the sum of $57,235, deducted by the commission on the legal theory there advanced is not tenable and that said sum should be restored. Likewise the item of $84,318 should be restored, since the engineer for the commission, for reasons appearing in the evidence, omitted certain items in his calculations which properly belonged therein. I therefore have concluded and found that value of account 1312 should be fixed at $1,294,710.

In relation to account 1314, it might appear that engineer Black's figure is an estimate based upon an arbitrary figure of 50 per cent of the depth of main lines for pipe lines and that Eastman, who testified for the company, was giving evidence from actual size, but a close examination discloses

that Eastman's unit prices which he was applying to field lines were not in accordance with the actual depth as shown by inspection, but that with the exception of field line ditches excavated by trench machines, he applied to his calculations of quantities the width and depth of ditches set forth in exhibit 73, as an average of all underground field pipe lines. I find nothing in the record to warrant setting aside the finding of the commission on this account number 1314.

Considering accounts 1325 and 1328 and 1331, which, among other properties, dealt with the Hog Shooter property, station and equipment account 1325, being as to land owned in fee except general land, account number 1376, account 1328 relates to station structures, and account 1331 relates to station equipment. In this connection it may be said that the argument advanced that between February, 1931, when the company for taxing purposes returned the Hog Shooter property as abandoned, and July, 1931, when the commission ordered the hearing, that the discovery of [fol. 416] new gas fields made the Hog Shooter station available, although still not in use during the hearing, does not favorably impress me, and I therefore conclude that $2,000 should have been deducted for the Hog Shooter property in account 1325, making the account valuation $145,202, and that $49,560 should have been deducted for Hog Shooter station structure in account number 1328, making the account valuation $1,466,102, and that in account 1331 the Hog Shooter equipment in the amount of $414,325 should have been deducted, making the account valuation $8,048,810.

Considering account 1333, the per cent condition of the property found to be 90.1 per cent by the commission, and the cost of rock excavation as found by the commission and approved by the majority opinion, and in that I concur, leaving only the quantities of rock excavated to be considered, and at the threshold of that consideration permit me to state that I agree with the majoriy that the overcuts should be excluded in connection with quantities of rock exeavated. It should be noted that since the hearing by the commission and before the trial by this court certain inspections were made on one line and the result of such inspection was introduced in evidence at the trial herein. But an examiation of that evidence so introduced discloses

nothing that will warrant this court in disturbing the finding of the commission in account number 1333, to wit $39,432,331.

Considering other valuations, I have discussed fully gas leases valued at $2,874,390 and the going-concern value fixed at $2,000,000.

I concur with the majority that cost of financing should not be included in the rate base.

There remains, therefore, only the following items, to wit: preliminary and organization expense, engineering and superintendence during construction, administration and [fol. 417] legal expense during construction, miscellaneous construction expenditures, taxes during construction and interest during construction.

Elsewhere in this opinion I have approved the principle of averaging the values as well as the earnings during the test period, but it should be noted that the valuations set out in the opinion are not average values. They are values of September 1, 1931. Using the valuation found as of that date, to wit, $73,409,190, I find that the plaintiff has failed to show that the 30 cent rate fixed by the commission is confiscatory.

Under the 40 cent rate the Cities Service Gas Company is earning 8.96 per cent a year upon the present value of its properties.

I find that on the valuation of $73,409,190 and at a rate of 30 cents the return would be 6.41 per cent. If averaged over a period for the calendar year 1930 and the year from June 30, 1930, to June 30, 1931, and the year from June 30, 1931, to June 30, 1932, the return of 30 cents would be 6.849 per cent.

Richard J. Hopkins, District Judge.

Conclusion

I conclude that the Plaintiff has not shown that the order of the Public Service Commission should be set aside and that the Bills should be dismissed.

[File endorsement omitted.]

[fol. 418] IN UNITED STATES DISTRICT COURT

DECREE—Filed Jan. 28, 1933

Now, on this 28th day of January, 1933, this case came on for decision pursuant to its previous submission to the court, the plaintiffs appearing by: James W. Finley, R. E. Cullison, Chas. Frueauff, Robt. S. Sloan, Fred Robertson, J. O. Emerson, Robt. Garver, Robt. Stone, and the defendants appearing by Walter T. Griffin, Chas. D. Welch, Harry Castor, Chas. W. Steiger and E. H. Hatcher, and thereupon, upon consideration thereof, it was ordered, adjudged, and decreed as follows:

(1) That the temporary injunction heretofore issued against the Attorney General of the State of Kansas be dissolved.

(2) That the temporary injunction restraining the defendant, The Public Service Commission of the State of Kansas, from enforcing its order of August 31, 1932, in so far as it pertains to the 1¾ per cent payment to Henry L. Doherty & Company, of the gross revenues of the distributing companies, be dissolved and that the application of plaintiffs for an injunction as to that part of said orders be denied and dismissed.

(3) That the defendants, the Public Service Commission of the State of Kansas, and the members thereof, and Roland Boynton, Attorney General of the State of Kansas, and each of them, their agents, servants, and employees, and all other persons acting under or through their authority, be and they are hereby permanently enjoined and restrained in the enforcement and execution of the provisions of two certain orders of said Public Service Commission dated August 31, 1932, insofar as the said orders require that the distributing companies, plaintiffs in the above named cases, should cease to set up on their books any payments made to Cities Service Gas Company for main line town border gas in excess of 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer, and, insofar as they and/or either of them require that effective September 1, 1932, and until a hearing is held and an order

[fol. 419] issued, the said distributing companies should charge rates to the consumers as follows:

All distributing companies paying a gate rate in excess of 30 cents per M. C. F. should deduct the difference between what the distributing companies were then paying at the city gate and 30 cents per M. C. F., and should pass this difference on to the consumer.

(4) That the costs in this court in these cases consolidate, be taxed one-half to the defendant, The Public Service Commission of the State of Kansas, and one-half to the plaintiffs.

The Public Service Commission of the State of Kansas and Roland Boynton, as Attorney General, defendants herein, hereby object and except to that part of finding number 13 which states:

"The present values are, on the extensive constructions of the last few years, less than the prudent investment therein. * * *"

and to each of findings Nos. 14, 16, 17, 18, 19, 20, 21 and to the conclusion of law No. 1 and to that part of this decree which enjoins the Public Service Commission of the State of Kansas in reference to its said orders, and exceptions thereto, are hereby allowed.

Plaintiffs and each of them object and except to findings Nos. 14 and 16 and exceptions thereto are hereby allowed.

Orie L. Phillips, Circuit Judge. Geo. T. McDermott, Circuit Judge.

Approved.

Jas. W. Finley, R. E. Cullison, Fred Robertson, R. D. Garver, Robert Stone, Attorneys for Plaintiffs. Chas. D. Welch, Chas. W. Steiger, E. H. Hatcher, Roland Boynton, Walter T. Griffin, Attorneys for Defendants.

[File endorsement omitted.]

[fol. 420] IN UNITED STATES DISTRICT COURT

ORDER SUBSTITUTING PARTIES DEFENDANT—Filed April 19, 1933

This matter coming on for hearing on the Motion of the State Corporation Commission and Homer Hoch, Jesse W.

Greenleaf and Ernest E. Blincoe, as members, that they be [fol. 421] substituted as parties defendant in the above entitled case, and the court being duly advised, finds that said motion should be sustained.

It is, therefore, by the Court ordered that the State Corporation Commission for the State of Kansas, and Homer Hoch, Jesse W. Greenleaf and Ernest E. Blincoe, as members of said Commission, be and they hereby are substituted as parties defendant in the above entitled action in the place of the Public Service Commission for the State of Kansas, and Jesse W. Greenleaf, Thurman Hill and Chas. W. Campbell, Commissioners.

Orie L. Phillips, Geo. T. McDermott, Richard J. Hopkins, Judge.

[File endorsement omitted.]

[fols. 422 & 423] In United States District Court

In Equity. No. 1637-N

[Titles omitted]

And the following cases consolidated therewith:

In Equity. No. 1638-N. In Equity. No. 1639-N. In Equity. No. 1640-N. In Equity. No. 1641-N. In Equity. No. 1642-N. In Equity. No. 1643-N. In Equity. No. 1644-N. In Equity. No. 1645-N. In Equity. No. 1646-N.

[fol. 424] Petition for Appeal, Assignment of Errors, and Prayer for Reversal.—Filed April 18, 1933

Petition for Appeal

To the Honorable District Court of the United States for the District of Kansas, First Division:

Your petitioners, The State Corporation Commission of Kansas, and Homer Hoch, Jesse W. Greenleaf and Ernest E. Blincoe, as members, successors to and substituted for The Public Service Commission of the State of Kansas, and

Jesse W. Greenleaf, Thurman Hill and Chas. W. Campbell, as members of said Commission, and Roland Boynton, Attorney General of the State of Kansas, the defendants in the above consolidated cases, considering themselves aggrieved by the decree entered in the above entitled cause on the 28th day of January, 1933, for the reason specified in the assignment of errors which is filed herewith, pray that they may be permitted to take an appeal therefrom to the Supreme Court of the United States at Washington.

Your petitioners further desire that an order be made fixing the amount of appeal bond herein for costs.

[fol. 425] ASSIGNMENT OF ERRORS

And your petitioners, The State Corporation Commission of Kansas, and Homer Hoch, Jesse W. Greenleaf, and Ernest E. Blincoe, successors to and substituted for The Public Service Commission of the State of Kansas and Jesse W. Greenleaf, Thurman Hill and Chas. W. Compbell, as members of said Commission, and Roland Boynton, Attorney General of the State of Kansas, defendants, assign the following errors in the record and proceedings in the said case:

1. The District Court of the United States for the District of Kansas, First Division, erred in permanently enjoining and restraining the enforcement and execution of the provisions of the two certain orders of The Public Service Commission as dated August 31, 1932, insofar as the said orders require that the distributing companies, plaintiffs in the above cases, should cease to set up on their books any payments made to the Cities Service Gas Company for mainline town border gas in excess of 30¢ per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

2. The Court erred in refusing to dismiss the plaintiff's bills of complaint and in granting the petitioners any relief.

3. The Court erred in their opinion and findings declaring the order of The Commission was, as to any part, unreasonable and would, if not enjoined, confiscate the property of these plaintiffs.

[fol. 426] 4. The Court erred in not accepting the finding of facts, declarations of law and dissenting opinion of Hon-

orable Richard J. Hopkins, as declaratory of the law and facts controlling in this case.

5. The Court erred in finding:

"The present values are on the extensive constructions of the last few years, less than the prudent investment therein * * *" (Finding 13).

6. The Court erred in finding the rate base to be $82,380,583. (Finding 14).

7. The Court erred in finding the present value of the Cities Service Gas Company's rights of way to be $1.62 per rod and erroneously increased the valuation in the amount of 22¢ per rod on rights of way, a total increase of $266,693.00. (Finding 14, Account 1307, 1327).

8. The Court erred in adding $84,318 to the cost of gas well construction as found by the Commission. (Finding 14, Account 1312), and thereby erroneously increased the rate base in said amount.

9. The Court erred in adding $397,017 to the value found by the Commission for production field line equipment, (Finding 14, Account 1314), and thereby erroneously increased the rate base in said amount.

10. The Court erred in finding that the Hogshooter compressor station was used and useful, and in adding to the value found by the Commission, $2,000 for land at the Hogshooter station, $49,560 for compressor station, and in adding the value of the equipment at the Hogshooter station in the amount of $414,925.00. (Finding 14, Accounts 1325, 1328, 1331.)

[fol. 427] 11. The Court erred in finding that the value found for Account 1333 by the Commission should be increased from $39,432,331 to $40,232,331, because the amount of rock excavation in the pipe-line construction allowed by the Commission was too law. (Finding 14).

12. The Court erred in finding that going concern value should be placed in the rate base at $5,000,000 and the value found by the Commission increased $3,000,000; (Finding 14).

13. The Court erred in finding that 1,261,000 acres of gas leases owned by The Cities Service Gas Company were used

and useful, and should be included in the rate base including developed, proven, probable and prospective acreage, and erred in increasing the acreage allowed as used and useful and in valuing the same at $5,727,272. (Finding 14.)

14. The Court erred in finding that the net income available for return amounted to only $5,800,327, and in including a portion of the rate expense of the present investigation as a proper item of expense in arriving at the net earnings available for return. (Finding 16.)

15. The Court erred in allowing $329,917 as annual replacement requirements on account of rentals on unproducing leases. (Finding 16.)

16. The Court erred in finding that $174,747.74 was necessary as an annual allowance for dry hole expense. (Finding 16.)

[fol. 428] 17. The Court erred in its finding and conclusion that The Cities Service Gas Company is earning an annual return of only 7.11 per cent on the present valuation of its property. (Finding 17.)

18. The Court erred in its finding and conclusion that approximately 8 per cent return upon present valuation is necessary for the Cities Service Gas Company at the present time, and that a return substantially lower than that would be confiscatory; and erred in its finding that if abnormality is considered the return must be increased and not decreased. (Finding 18.)

19. The Court erred in its finding that under the orders of the Commission, the return upon the properties of The Cities Service Gas Company dedicated to the public use would be 4.8 per cent; and erred in its finding that such rate under present conditions is confiscatory. (Finding 19.)

20. The Court erred in its finding that if the distributing companies are compelled to pay 40c per thousand cubic feet for gas at the city gates and to base their rates to consumers upon the price fixed as reasonable by the Commission, no one of them will have earnings in excess of operating expenses applicable to depreciation and return. (Finding 20.)

21. The Court erred in its conclusion of law that that portion of the first order of the Commission, made August [fol. 429] 31, 1932, providing that the distributing companies should give no consideration to the payments for gas at the city gates in excess of 30c per thousand cubic feet in fixing the rate for domestic consumers, should be permanently enjoined. (Conclusion of law, 1).

22. The court erred in its conclusion that forty cents per thousand cubic feet for gas at the city gates is a reasonable charge. (Opinion.)

[fol. 430] Prayer and Reversal

For which errors the petitioners, The State Corporation Commission of the State of Kansas, and Homer Hoch, Jazza W. Greenlief and Ernest E. Blincoe, as member of said Commission, and Roland Boynton, as Attorney General of the State of Kansas, pray that said judgment and decree of the District Court of the United States for the District of Kansas, First Division, dated January 28, 1933, in the above entitled cause, be reversed in so far as it enjoins the enforcement of any part of the Commission's said orders, and a judgment rendered in favor of said petitioners, and for costs.

Chas. D. Welch, Louis R. Oates, Chas. W. Steiger,
E. H. Hatcher, Roland Boynton, Atty General,
Counsel for Appellants.

Received copy of the foregoing petition for appeal, assignment of errors and prayer for reversal, this 12th day of April, 1933.

Robt. D. Garver, Robt. Stone, Counsel for Appellees.

[fol. 431] In United States District Court

Order Allowing Appeal. Filed April 19, 1933

The Appellants in the above entitled suit and each of them, having prayed for the allowance of an appeal in this cause to the Supreme Court of the United States from the judgment and decree made and entered in the above en-

titled suit by the District Court of the United States for the District of Kansas, First Division, on the 28th day of January, 1933, and having presented and filed their petition for appeal, assignment of error, and prayer for reversal pursuant to the statutes and the rules of the Supreme Court of the United States in such case made and provided;

It is now here ordered that an appeal be, and the same is hereby allowed to the Supreme Court of the United States from the District Court of the United States for the District of Kansas, First Division, in this cause as provided by law; and it is further ordered that the Clerk of the court appealed from shall prepare and certify a transcript of the record, proceedings, judgment and decree in this cause and transmit the same to the Supreme Court of the United States.

And it is further ordered that security for costs on appeal be fixed in the sum of $5,000.00, and that bond be given therefor.

Dated this 19th day of April, 1933.

Orie L. Phillips, Circuit Judge. Geo. T. McDermott, Circuit Judge. Richard J. Hopkins, U. S. District Judge.

[File endorsement omitted.]

[fols. 432-434] Bond on appeal for $5,000, approved and filed April 18, 1933, omitted in printing.

[fol. 435] IN UNITED STATES DISTRICT COURT

Condensed Statement of Evidence Essential to Decision on Question Presented on Appeal—Filed May 15, 1933

The case was tried below to a statutory three-judge court, the evidence introduced consisting of the entire record of evidence introduced by all parties before the Public Service Commission of Kansas, such record consisting of approximately 3000 pages of testimony and 103 exhibits, and certain additional stipulations and affidavits considered as evidence by the parties.

Issues

The issues for determination before the Commission and the Court below were as follows:

1. The reasonableness of the price charged by the Cities Service Gas Company to the several distributing companies, respondents before the Commission and plaintiffs below.

2. The reasonableness of the contract between Henry L. Doherty & Company and said several distributing companies under which they paid for certain services, 1¾ per cent of their gross revenue.

3. The reasonableness of the contract between said several distributing companies and The Gas Service Company.

[fol. 436] This appeal concerns only issue No. 1, above, as to the reasonableness of the price charged for gas at the city gates of the respective cities served by the appellees, neither party having appealed from the decision of the court below as to other issues.

The Court below in its findings of fact considered the several elements entering into the rate base of the Cities Service Gas Company under certain account numbers and headings and this condensed statement of the evidence will follow such divisions of the subject, so far as possible.

Stipulation as to Certain Facts, Testimony, etc.

The parties stipulated before the District Court as follows:

"It is hereby stipulated by the parties that the three instruments marked respectively, A. B. and C. by the reporter are the three orders made by the Texas Railroad Commission with regard to permissible takes from wells in the Amarillo field of Texas.

"It is further stipulated that a suit has been brought in the Federal Court in Texas, contesting the validity of this order and that the same was restrained by the Court, set for hearing in the matter on application for temporary injunction, that subsequent to the issuance of said restrain-

ing order the Texas Commission set aside the order of September 15th, for the reasons set out in Exhibit 3.

"It is agreed by the parties that the witness, H. O. Caster, a member of the Executive Committee of Henry L. [fol. 437] Doherty & Company and the head of the Natural Gas Division of that organization will testify that all leases in present gas reserves of the Cities Service Gas Company were purchased in the exercise of the bona fide business judgment of himself and other members of said Executive Committee, and the managing officers of the Cities Service Gas Company as necessary to secure an adequate supply of gas for the Cities Service Gas Company and were not purchased for speculation.

"It is further agreed by the parties that the witness, Ross M. Stuntz, Superintendent of Gas Production of the Cities Service Gas Company, will testify that all of the present reserves of the Cities Service Gas Company are, in his opinion, presently necessary to the Cities Service Gas Company; that at the present time the Cities Service Gas Company owns 111,574 acres of producing leases, that 5 percent of all gas transported through the Cities Service Gas Pipe Line System is necessary for leakage and the operation of compressor stations and cannot be figured in deliveries to consumers; that in computing the number of acres comprising the above figure of 111,574 as representing producing leases, the computation was made on the basis of one well rendering a lease developed, without regard to the size of the lease, and that if a well is located on an eighty acre lease, eighty acres are included as productive and if the well is located on a thousand acre lease the same is true, except in the Osage Nation of Oklahoma where the company owns one lease of 181,120 acres, of which 2,480 acres are classed as producing, although there are 14 wells on the 181,000 acres block as a whole. That the above developed acreage is divided between the states as follows: Texas, 97,700 with 60 wells as of September 1, 1931, and 2 additional wells since that time, making a total of 62 wells; Kansas 10,071 acres with 189 wells as of September 1, 1931; Oklahoma 3,613 acres developed with 40 wells as of September 1, 1931.

[fol. 438] "It is further stipulated that the witness, H. O. Caster, will testify that in his bona fide business judgment the contract under which the distributing companies, com-

plainants herein, pay to Henry L. Doherty & Company one and three-fourths percent of their gross revenues is to the best interest of said distributing companies and that services are rendered to said companies which are necessary or advisable to their operations and that such services cannot be procured elsewhere at a less cost to said company, and that the same is true with respect to a like contract between Henry L. Doherty & Company and the Cities Service Gas Company.

"It is further stipulated that the witness F. C. Hamilton will testify that he is familiar with the value and financial experience of the distributing companies, plaintiffs herein, and that the value of their respective properties and their operating experience is as set out in the several bills of complaint of the complainants herein other than the Cities Service Gas Company, to which the Public Service Commission objects on the ground that the testimony is irrelevant, incompetent and immaterial, and further states that it has had no opportunity to investigate this matter or value the property and that it was the intention of the Commission to do so in pursuance of its order set out in plaintiff's bill of complaint at Exhibit 1.

"It is further stipulated that the witness F. C. Hamilton will testify that if the several distributing companies complainants herein are compelled to pay the price they are now paying the Cities Service Gas Company for gas at their respective city gates and are compelled to base their rates to consumers upon the price fixed by order, Exhibit M, they will not be able to make operating expenses, with nothing for return and depreciation on the value of their property, to which testimony the Commission objects [161, 439] on the ground of incompetency, the subject matter not coming in issue until the Commission has made an investigation for the purpose of determining the fair value of the properties owned by the distributing companies and their rate of return.

"It is further stipulated that the witness James A. Emery will testify that he is Vice President and Director of Ford, Bacon & Davis, Inc., engineers; that he was employed by the complainants herein to make a study of the property of the Cities Service Gas Company for the purpose of determining the proper allowance for going value and that in the opinion of said witness going value should

be allowed in a sum between eight and a half and nine million dollars.

"It is further stipulated by the parties that the Exhibit marked 4, which is an abstract of the testimony before the Commission in regard to the contract of Henry L. Doherty & Company *in regard to the contract of Henry L. Doherty & Company* prepared by the parties may be considered by the Court with the eliminations of any statements which appear therein which may not properly be considered as an abstract of the testimony.

"It is further stipulated by the parties that the entire record and all exhibits before the Commission may be considered by the Court herein without regard to whether or not the evidence is abstracted.

"If is further stipulated that the contract between the Cities Service Gas Company and Henry L. Doherty & Company under which it pays one and three-fourths percent of its gross revenue on sales to unaffilliated companies and pipe line customers not served through distributing companies and was entered into in like manner and that H. O. Caster and H. R. Straight, General Manager of Cities Service Gas Company would testify that there is no species of domination or control over Cities Service Gas Company by any person, company or corporation other than [fol. 440] such as necessarily arises by ownership of all voting stock except qualifying shares and by Empire Gas & Fuel Company, and as may be implied, if any, by the management contract above mentioned.

"It is further stipulated that there is no contract between Gas Service Company and Henry L. Doherty & Company, under which it pays them one and three-fourths percent of its gross earnings or any other compensation whatever.

"It is further stipulated that the cost of the leases, sold to the Texhoma and transferred in August, 1931, as shown by the books of the company, is $846,217.72.

"It is further stipulated that all affidavits introduced by any of the parties are subject to objection for relevancy and materiality.

"It is stipulated in connection with the affidavit of H. L. Montgomery that the city gate rate of the Cities Service Gas Company in Oklahoma is 35 cents.

"It is agreed that if the rate established by the Commission in its order Exhibits L. — H., if applied to the

business of the Cities Service Gas Company for the year ending June 30, 1932, would result in a reduction of earnings of $1,926,145.07, leaving net earnings above replacement reserves of $5,935,377.78.

"It is stipulated that exhibit 5 is a photostatic copy of one of the storage leases in effect in the Craig field and that the photostatic copies of checks attached thereto are checks that were paid in connection with said contract.

"It is further stipulated that the same form of contract was executed by all land owners in this field. As to the Eldorado field referred to in the record as the Augusta field the Cities Service Gas Company was the owner of production leases covering all land now used for storage, which leases provided for annual payment per well during such time as gas was used off the premises and that the com- [fol. 441] pany is continuing to pay the land owners the stipulated rental per well the same as if gas were being produced from the sand instead of from storage. There is no additional contract with the land owners who are receiving and accepting their annual rentals the same as if gas was actually being produced. The leases under which the storage field is now held are the ordinary form of oil and gas leases providing for annual rental per well for gas used off the premises.

"It is further stipulated between Cities Service Gas Company and defendants in its case that said company could not continue its business without the patronage of the defendant distributing companies."

It was stipulated between the parties that an agreed statement of facts and agreed abstract of the evidence should be presented to the lower court with the evidence pertaining to each account brought forth and abstracted under each particular account of the valuation to which it pertains. The valuation for a large number of the accounts is not in controversy before the district court and is not in controversy in this appeal.

The parties stipulated as follows:

"The foregoing is agreed to be a correct abstract of the evidence introduced before the Commission in the proceedings in question and all facts herein stated may be considered as shown by the evidence without prejudice to the introduction of additional evidence by any party."

Agreed Statement of Facts and Evidence

The agreed statement of facts and the agreed abstract of the evidence setting forth the undisputed accounts is as follows:

"In its order of July 20, 1932, the Public Service Commission found the value of the property of the Cities Service Gas Company and associated companies to be $73,051,-[fol. 442] 235.00 as of September 1, 1931.

"In its order of August 3, 1932, the Commission made additions to its previous finding and found the value of this property as of September 1, 1931 to be $73,148,510.00. In making this finding of value, the Commission intended to add $119,275.00 to the value previously found, but by mistake added the sum of $119,275.00 to the figure of $73,029,-235.00 instead of adding it to the figure of $73,051,235.00 as previously found. The correction of this error makes the value of the property of the Cities Service Gas Company, as of September 1, 1931, as found by the Commission, $73,170,510.00.

"On pages 28 and 29 of the opinion, the Commission tabulates by account numbers the several items entering into its valuation as found, and the evidence as hereinafter abstracted will follow the account numbers as tabulated by the Commission and followed in its opinion.

"The witnesses who testified in regard to valuation were F. C. Hamilton, consulting engineer for Henry L. Doherty & Company, and H. L. Eastman, associated with Mr. Hamilton, for the respondents, and E. B. Black, of the firm of Black and Veatch of Kansas City, Missouri, for the Public Service Commission. In the following abstracts these witnesses will be referred to as Hamilton, Eastman and Black. All based their present value on reproduction cost, new, less depreciation.

"Mr. Black testified: 'It was not my idea in making this appraisal or fixing these prices to use the rock bottom price of labor or materials.'

"C. H. Montgomery, the Certified Public Accountant employed by the Commission, testified as to exhibits prepared by him, included in which is the value of the property of the Cities Service Gas Company as shown by its books.

"The correctness of Montgomery's audit is not questioned. As shown in the exhibit offered by him the cost of

the gas leases, owned by Cities Service Gas Company, is $6,573,489.70. This figure is also recited by the Commission in its opinion at page 118. The plant investment and [fol. 443] other assets including leases of Cities Service Gas Company is shown in the same exhibit to be $96,795,538.93 and at page 1970 of the record at $96,795,000.00. This figure includes some leases later sold to the Texhoma Company.

UNDISPUTED ACCOUNTS

"Account No. 1307. Production—Rights of way. In his valuation, Black separated production right of way and transmission right of way, whereas Hamilton included both under Account No. 1327. The testimony of both Black and Hamilton will be abstracted under Account No. 1327.

"Account No. 1310. Production—Field measuring station structures—$35,909.00.

"Account No. 1311. Production—Other structures—$47,876.00.

"Accounts Nos. 1315. Production—Field measuring station equipment—$265,746.00.

"Account No. 1317. Production—Other Equipment—$1,333.00.

"Account No. 1329. Transmission—Measuring Station structures—$133,310.00.

"Account No. 1330. Transmission—Other structures—$113,341.00.

"Account No. 1332. Transmission measuring station equipment—$759,625.00.

"Account No. 1334. Transmission—Other equipment—$5,633.

"Account No. 1379. General—Other structures—$94,687.00.

[fol. 444] "Account No. 1384. General—Garage equipment—$81,448.00.

"Account No. 1386. General—Telephone and Telegraph system—$415.070.00.

[fol. 445] "ENGINEERING AND SUPERINTENDENCE

"The parties agree that 5% of the physical value of the property of the Cities Service Gas Company, except Accounts Nos. 1316, 1380, 1381, 1382, 1383, 1384, 1385, 1387

and 1388, should be used in estimating the value of engineering and superintendence. The Commission used 5% in its calculation and no contention exists as to this item except if any change is made in the valuation as found by the Commission as to accounts other than those herein recited this account should be adjusted accordingly.

"Taxes During Construction

"The Commission's allowance of $778,044.00 for this account is accepted by the parties.

"Cost of Financing

"Hamilton included in his valuation $3,422,512.00 for this item, that figure being based on 4% of the total value of the property including interest during construction and that, in his opinion, the expense was an actual one bound to occur in the reproduction of the property. Black testified that, in his opinion, the allowance was improper and did not include it in his valuation. The Commission disallowed the item in its entirety.

"Working Capital

"The allowance of $775,000.00 made by the Commission is accepted by the parties.

"Material and Supplies

"Hamilton testified that materials and supplies on hand September 1, 1931, according to the books of the company, amounted to $548,096.00. Black testified that he took the average cost of materials and supplies on hand June and September 1, 1931, of $509,400.00, as shown by the books of the company.

[fol. 446] "The difference between the materials and supplies on hand September 1, 1931, and an average of such supplies as of June 1 and September 1, 1931, is $57,496.00.

"Miscellaneous Construction Expenditures

"This item is discussed by the Commission at page 84 of its opinion. For the purposes of this agreement we have included it under the subsequent heading Organization Expenses, Legal and Administration Expenses During Construction and Miscellaneous Construction Expenditures.

"Organization Expense, Legal and Administration Expenses During Construction, Miscellaneous Construction Expenditures

"These three items are considered separately by the Commission in its opinion at pages 83 and 84. Black and Hamilton, in their respective valuations, used slightly different percentages applied to different classifications but arrived at approximately the same result and made allowances for all of the items totaling approximately 2% applied to the respective physical values found by them plus allowances for engineering and supervision. For the purpose of this case, it is agreed that 2% is a proper allowance for the several items to be applied to the total of the physical value found by the court plus its allowance for engineering and supervision."

[fol. 447] Disputed Accounts

The following accounts are in controversy on appeal:

Account No. 1312. Production—Gas well construction.

Account No. 1313. Production—Gas well equipment.

It was agreed by the parties before the District Court that:

"Black testified to a value of $1,718,813.00 new and $1,210,-392.00 depreciated for the Account No. 1312 and $658,245.00 new and $484,514.00 depreciated for Account No. 1313. Hamilton testified to a value new of $2,022,296.00 and $1,300,-025.00 depreciated for Account No. 1312 and $917,777.00 new and $573,124.00 depreciated for Account No. 1313. These two accounts are combined in this abstract in order to get comparable figures for the reason that in the evidence testi-

mony is given as to the cost to the company of wells, including equipment.

"The Commission in its opinion reduced Black's figures for Account No. 1312, $130,363.00 new and $57,233.00 depreciated, being the value placed on gas well construction (the hole) for storage wells by Black. A storage well is one which was formerly drilled for gas and has been converted into storage use. The company has two fields which it uses for storage, one known as the Craig field and the other known as the Augusta field. The fields are used as reservoirs into which gas is injected through storage wells [fol. 448] during the summer months when the demand for gas is low, as a reserve to be used when the demand is greater. The record shows that the company after these fields had been nearly depleted, leased these lands from the owners for storage purposes at a yearly rental.

"The Commission disallowed the value of these wells insofar only as the value referred to the hole, on the ground that these wells (referring to the hole only) belong to the landowners, the lessor, and not to the company, and are simply leased to the Company for the purpose mentioned in the storage lease, and that the Company has no title to them.

"To Black's figure for Account No. 1313 the Commission added $236,373.00 new and $173,925.00 depreciated because the prices Black applied to casing and tubing in the wells was considered insufficient. The Commission finding as follows: "The testimony with respect to the allowances for casing and tubing included in this account is apparently conclusive with respect to the prices fixed by Black being insufficient, while the testimony is not conclusive that the prices used by Mr. Hamilton were representative prices as of the date of his valuation. However we have accepted his total of $853,309.00 for casing and tubing in this account, corrected for overheads included, which we believe to be excessive, and have applied instead the overheads used by Mr. Black."

"The allowance by the Commission for Account No. 1312 is $1,588,450.00 new and $1,153,157.00 depreciated. For Account No. 1313, $894,618.00 new and $658,439.00 depreciated, making a total of the two accounts of $2,483,068.00 new and $1,811,596.00 depreciated. This compares with Hamilton's [fol. 449] value for the two accounts of $2,940,073.00 new

and $1,953,149.00 depreciated, leaving a difference between the Commission's finding and the amount estimated by Hamilton of $457,005.00 new and $141,553.00 depreciated.

"In addition to the estimates of Black and Hamilton contained in their respective valuations, testimony was given by Eastman as to the actual cost to the Cities Service Gas Company of certain wells in representative fields together with testimony as to the cost of adjacent and comparable wells drilled and owned by other companies. This testimony is summarized in the following tabulation:

	Total cost	Depth	Date drilled	Record page
Hobbsville Field				
Fish No. 2 C				
Hamilton	$27,469.00	2932	Dec. 1930	Exh. #17
Black	16,880.98			2534
Actual Cost to Company	30,075.76			2534
Cost of Adjacent Wells drilled by other Companies				
Tiger #1, Midcontinent Pet. Co.	36,193.43	2934	July 1931	2535
Smith #1, Minnehoma O. & G. Co.	35,014.16	2927	Aug. 1930	2535
Smith #2, Minnehoma O. & G. Co.	31,439.63	2922	Apr. 1931	2535
Brown #1, Winona Oil Co.	36,456.30	2949	Oct. 1930	2535
Street #1, Winona Oil Co.	33,376.44	2922½	Jan. 1931	2535
Elias #1, Texas Co.	30,726.44	2895	Aug. 1930	2537
Average of above six wells	35,197.73	2925		
Little River Field				
Charty No. 2				
Hamilton	39,326.00	3128	Sept. 1929	Exh. #17
Black	21,280.62			2538
Actual Cost to Company	42,567.44			2538
Cost of Adjacent Wells drilled by other Companies				
Alec #3, Midcontinent Pet. Co.	37,641.48	3165		2538
Alec #1, Carter Oil Co.	43,493.05	3117	Apr. 1929	2540
Factor #1, Carter Oil Co.	*59,531.69	3090	Apr. 1929	2540
Gotcha #13, Gypsy Oil Co.	43,607.15	3152	June 1929	2540
Gotcha #15, Gypsy Oil Co.	37,506.26	3114	July 1929	2540
Janney #7, Texas Co.	38,803.75	3159	July 1929	2541
Haney #2, Sinclair O. & G. Co.	44,791.06	3126	May 1930	2541
Smith #6, Prairie O. & G. Co.	31,937.93	3205	Mar. 1930	2541
Average of above eight wells	42,164.04	3140		

* Erroneously reported in record as $159,531.69.

[fol. 450]

Perry Field:				
Freyler No. 1				
Hamilton	$45,117.00	3467	Oct. 1930	2542
Black	24,899.88			2542
Actual Cost to Company	50,530.22			2542

Freyler No. 2				
Hamilton	44,464.00	3449	Nov. 1930	2587
Black	24,570.87	.....	.....	2586
Actual Cost to Company	49,248.74	.....	.....	2587
Cost of Adjacent Wells Drilled by Other Companies:				
McCormick #1—Indian Territory I. O. Co.	53,417.00	3387	.....	2588
McCormick #2—Indian Territory I. O. Co.	53,417.00	3367	.....	2588
Walter Meyer #1 Sinclair Oil & Gas Co.	51,430.55	3421	Oct. 1929	2588
Walter Meyer #1 Prairie Oil & Gas Co.	47,081.60	3437	May 1929	2589
Trussel #1 Twin City Oil Co.	51,828.36	3450	Oct. 1930	2589
Stewart #1 Twin City Oil Co.	*39,680.15	3405	Mar. 1931	2589
Average of above six wells	49,475.78	3411	.....	....

* Difference in cost of Trussel and Stewart Wells was due to use of fuel and water lines of the former well in the drilling of the later without proper distribution of charges. See Record, page 2589.

Average cost of Trussel & Stewart, 45,754.26.

Amarillo Field:				
Fuqua No. 2				
Hamilton	24,981.00	2736	.....	2595
Black	19,843.34	.....	.....	2590
Actual Cost to Company	30,197.13	.....	.....	2590

"In addition to estimates of Black and Hamilton and testimony by Mr. Eastman, Mr. Richie, production manager for the Derby Oil Company and theretofore production and pipe superintendent of the Marland Oil Company, having had fourteen years' experience in drilling and contracting wells in Kansas, Oklahoma, Texas, New Mexico and California, testified that he was familiar with costs of drilling wells in the Amarillo Proven Sweet Gas fields in September, 1931; that by use of rotary tools, wells could be drilled in this field at this time at a less cost than if standard tools were used, and that the Fuqua Well No. 2 and the Burnett Well No. 14, concerning the former of which respondent introduced testimony as to their actual cost, could be completed at which is [fol. 451] known as turn-key job prices as follows: The Fuqua Well No. 2 at $22,303.00 with standard and $22,101.00 with rotary tools; and that the Burnett well No. 14 could be completed for $27,301.00 with standard and $23,779.00 with rotary tools. Mr. Black's complete costs on these two wells are as follows: Fuqua well No. 2, $19,843.00 and Burnett well No. 14, $30,024.00 and total considerably more than Mr. Richie testified it would actually cost to complete these wells.

"In addition Mr. Richie stated that if he had twenty wells to drill his cost would be reduced five per cent.

"A comparison of Mr. Black's, Mr. Hamilton's and Mr. Richie's valuation of certain wells, completely equipped, is found on transcript page 2891, and follows herewith:

Well	Black	Hamilton	Richie Standard rig	Richie Rotary
Fuqua No. 2	$19,843	$24,991	$22,303	$22,101
Burnett No. 14	30,024	32,847	27,301	23,779."

Eastman testified for the Company in substance as follows:

Gas well construction includes drilling of gas wells, that is, the cost of the hole; exclusive of cost of material.

Burnett Well, No. 13, shows depth of well to be 3,180 feet. The cost per foot to be $6.57; contractors price for drilling per foot, $3.50; to that is added $3.07 to cover company labor and incidental expenses making total unit cost per foot of $6.57.

Witness had no detailed items of company labor, just divided $759.00 by the average depth of the wells drilled during the period from 1925 to 1931 in that field, making 28 cents per foot. The Burnett well was drilled in 1925. [fol. 452] The contract price for drilling a well in 1929 as compared with 1931 was higher. Did not know how much, but had in mind 25 to 30 percent at the time; $3.50 per foot is the common ordinary price for drilling a well in the Aramillo field in 1931. Approximately $1.75 of the unit price is made up of what is termed incidental expenses of the company and contractor. He could not give individual items which go to make it up. One item is $1.04 payment per day for cleaning and rigging up the well after it is drilled. The above is the average unit cost price of twenty-three wells in the Amarillo field.

Eastman testified that he had made a study of the actual cost of wells drilled by the Cities Service Gas Company for the purpose of comparing such actual costs with the estimates of Hamilton and himself as contained in their valuation and the estimates of Black as contained in his valuation.

That on page 349 of Black's valuation he shows the T Buck No. 1 well in Hughes County, Texas, in which the company has a 50% interest as $6,289.00 for the half interest or $12,578.00 for the well; that he has letters from drilling contractors showing the cost of drilling quoted

at $5.00 and $5.50 per foot for drilling only exclusive of fuel, water, day labor and all incidental expense; the depth of that well is 2,481 feet; that taking $5.00 a foot, the lowest cost quoted for drilling, the drilling cost of the well would be $14,905.00. To that figure would have to be added all day labor, fuel, water and other incidentals; that the figure used by Hamilton and Eastman in their value for this well is $24,991.00, practically double the figure used by Black; that the bare drilling cost alone is in excess of the total cost allowed by Black.

That Black has included for Fish No. 4 well $12,921.00; that drilling quotations from contractors are $5.00 and [illegible] $5.50 per foot; that the depth of the well is 2,932 feet; that the drilling of this well at $5.00 per foot would cost $14,460.00 as against the figure of $12,921.00 allowed by Black for all expense. The witness introduced in evidence a photostatic copy of the job order of the company covering this well which shows the total cost of the well to the company to be $30,073.76. This figure is comparable to Black's total figure for labor and material of $16,000.91. The well was drilled in December, 1930. In this connection the witness introduced a letter from the Mid Continent Petroleum Company showing the cost of their wells known as Louisa Tiger No. 1 and George Aloe No. 3 in the same locality. The Tiger well is close to the Fish well, was drilled July 2, 1931, the total cost was $30,193.43 and the depth of the well 2,934 feet or two feet deeper than Fish No. 2. The witness also produced a letter from the Minnehoma Oil & Gas Company showing the cost of drilling their Smith No. 1 and No. 2 wells. The cost of Smith No. 1 well was $35,014.16 and the depth 2,927 feet. Smith No. 2 is 2,922 feet deep and the cost is $31,439.63. Smith No. 1 was drilled August, 1930, and Smith No. 2 April, 1931. The witness also produced a letter from the Winona Oil Company showing the cost of Jenny Brown No. 1 and Street No. 1 in the same field drilled within the last fifteen months. Brown No. 1 cost $36,456.30 and was drilled in October, 1930, to a depth of 2,949 feet. Street No. 1 cost $33,376.44, was drilled in January, 1931, to a depth of 2,922½ feet. The witness also produced a letter from the Texas Company showing cost of drilling their Burkholder No. 7, Eliza No. 1 and Janney No. 7 wells. Only one of these wells was in the same field—

Ellen No. 1, drilled in August, 1930, to a depth of 2,895 feet at a total cost of $30,726.44; that the witness went to these other companies for the purpose of finding out how their experience tallied with the experience of the Ellis Service Gas Company.

[fol. 454] Charty Well No. 2 is included in Black's valuation, page 349, at a total cost of $21,200.02, his figure for drilling, fuel, water and incidental expense being $15,416.00 and his equipment $5,784.02. This well is in the Little River Field in the Seminole area. The witness had quotations from four contractors in the Little River Field, the minimum bid for drilling being $5.00 per foot as of September 1, 1931, and the high bid of $6.50. The drilling alone for this well, figured at $5.00 per foot, would be $15,040.00 which is in excess of the figure used by Black for the completed well (exclusive of equipment). The witness produced photostatic copies of the records of the company showing actual cost of drilling and equipping Charty Well No. 2, which was introduced as Exhibit 67. The actual cost of this well, as shown by the records, was $42,507.00 or $20,000.00 in excess of the figure used by Black. For the purpose of comparison, the witness procured information from the Mid Continent Petroleum Corporation as to the cost of its Alec No. 3 in the same field. The well was drilled to a depth of 3,165 feet and cost $37,641.48. The Carter Oil Company's well, Alec No. 1, cost $43,493.05 and was drilled to a depth of 3,117 feet. The T. Proctor No. 1 well of the same company was drilled to a total depth of 3,080 feet and the cost was $159,531.62. The witness also produced a letter from the Gypsy Oil Company reporting the cost to it of two wells in the same field. M. Cotcha Well No. 13 cost $43,607.15 and was drilled to a depth of 3,152 feet. The Cotcha Well No. 15 cost $37,506.26 and was drilled to a depth of 3,114 feet. These wells were drilled in June and July of 1929. The Janney Well No. 7 of the Texas Company in the same field was drilled in July, 1929, to a depth of 3,170 feet and cost $38,803.75. The witness also produced a letter from the Sinclair Oil & Gas Company reporting the cost of drilling its Haney No. 2 well in the same field to be $44,791.16, the well being drilled in May, 1929, to a depth of 3,126 [fol. 455] feet. A letter from the Prairie Oil & Gas Company reported the cost of drilling its Bert Smith No. 6

well drilled in March, 1930, to a depth of 3,205 feet, to cost $31,937.93.

At page 350 of Black's valuation he lists the Freyler Wells Nos. 1 and 2; he gives the cost of these wells, exclusive of equipment, at $17,630.00 for No. 1, with $7,269.88 for equipment, making a total of $24,899.88. The lowest quotation from drilling contractors for drilling in this field is $5.50 per foot. The depth of Freyler No. 1 is 3,467 feet and the drilling alone would cost $19,068.50 as compared with Black's $17,630.00. A photostatic copy of the company's record showing the actual cost of this well was introduced in evidence showing the cost to be $50,530.29 as compared with Black's figure of $24,899.88 more than double the amount allowed by Black.

Eastman further testified that in preparing the unit costs which were used by Hamilton and himself in Hamilton's valuation he studied and analyzed the actual cost of the company in drilling wells in the several fields and by dividing such actual costs into the number of feet drilled arrived at a unit cost per foot which was adjusted for material and labor to present prices and then applied to the several wells.

The cost figures of the company quoted by Eastman include New York engineering overheads, right of way and miscellaneous expenses. Black included engineering and miscellaneous expense as separate items in his general overhead, and right of way in Account No. 1307.

Black testified for the Commission that the cost of drilling the Fuqua Well No. 2 as estimated by him, to be $14,834.00. That is, $4.00 is the drilling price; day work is allowed for in the total price as follows: 3 days at $80.00 per day; for fuel and water for drilling 45 days at $35.00 [fol. 4567] per day; depreciation of casing withdrawn and used $1,650.00; transportation of casing and tubing $200.00; superintendence for 45 days at $5.00, making the total of $14,834.00. The $4.00 just covers the drilling of the hole and placing the casing, etc.

A. S. Richis, of Wichita, Kansas, witness for the Commission, testified in substance as follows:

At the present time he is Vice-President of the Derby Oil Company in charge of production and pipe lines, which

Company is engaged in the business of production of oil, refining and marketing of same, also in the production of natural gas for sale purposes. He is familiar with the business and has been for fourteen years. For ten and one half years, he was employed by the Marland Oil Company in the production division in the states of Kansas, Oklahoma, Texas, New Mexico and California. He is familiar with the Amarillo gas field, had supervision of the development in that field from the general office in Ponca City, but was not actually on the ground all the time; that he is familiar with the cost of drilling gas wells in Carson County in the Amarillo field as of September, 1931. He has made calculations of actual cost of drilling Fuqua No. 2 well in Carson County. He has made an estimate of the cost of drilling and equipping, furnishing the drilling equipment, labor, water and fuel, and turning said well over as a complete turn key job as of the date of November, 1931.

"The first item is the rig, $3,250.00, tanning, labor and construction of ponds $950.00, that makes a total of $4,200.00 for the rig, you understand this is a regulation, standard job. I have made this estimate on casing at 122 feet of 20 inch, 90 pound, $5.75 a foot, $736.00; 244 feet of 15½ inch, 70 pound, at $4.50 a foot, $1,098.00; 2,251 feet of 8¼ inch, 32 pound at $1.50, $3,445.50. I have included 2,700 feet of 2 inch, 4½ pound tubing at 22 cents, welding on the above casing depreciation on the above [fol. 457] casing $594.00, for the tubing, the welding on the casing including tubing $250.00, fuel 42 days at $15.00 per day, $630.00; water, ten dollars per day for 42 days, $420.00; 2,736 feet of hole at $3.50 per foot, $9,576.00; five days of 24 hours each day work at $80.00 per day, $400.00; miscellaneous tanks, pipe fittings and supplies, a figure of $600.00; well connections for shutting in after completion, $470.00; fence for enclosing well after completion, $58.00; miscellaneous labor and hauling, teaming that has to be done around during the work, estimated figure of $600.00; $150.00 overhead; a gross figure of $25,[illegible]. From that I have deducted the following items as salvage of rig, material only, removed from the property, with credit of $2,437.50, on your item of miscellaneous [illegible]

pipe fittings, etc., $300.00, total salvage $2,737.50, leaving a net after salvage of $22,303.50. That is estimated with standard cable tools.

"I would drill this well with rotary tools and have made an estimate of the cost of drilling this well with rotary tools, which is as follows:

"Rig material $3,500.00; pond, labor and trucking, $1,050.00; 244 feet of 12½ inch casing, $610.00; same valuation per foot as on the other, 2,297 feet of 8¼ casing, $2,445.50; 2,700 feet of two inch tubing, 4½ pound tubing, $594.00; welding on the above casing including the tubing $125.00; fuel, 20 days at $30.00 per day, $600.00; another item of fuel there of five days at $15.00 per day, for a total of $75.00; water, 20 days at $50.00 per day, $1,000.00; another item on water, five days at $10.00 per day, $50.00; contract 2,736 feet at $4.25 a foot, $11,628.00; three days day work, 24 hours each at $90.00, $270.00; miscellaneous tanks, fittings and connections and supplies $700.00; well connections $470.00; fence $58.00; cement and cementing, that is the cement and cost of cementing, $400.00; miscellaneous labor $300.00; overhead $150.00; for a gross of $25,025.50; [fol. 458] your salvage column, a figure of $2,625.00 for the rig, in your item of miscellaneous tanks, fittings and supplies, salvage of $300.00, or a total of $2,925.00 salvage, making a net for the job, after salvage of $22,100.50.

"That the cost of the rotary method would be $22,100.50, with the standard tools, $27,302.50. That he has also made calculations of a turn-key job for the full completion of the Burnett Well, No. 14, which is as follows:

"Rig material $3,250.00; labor, ponds, teaming, and trucking $950.00; casing, 260 feet of 20 inch, 90 pound, $1,495.00; 648 feet of 15½ inch, 70 pound, $2,916.00; 1115 feet of 12½ inch 50 pound, $2,787.50; 2,150 feet of 10 inch, 40 pound, $4,300.00; hauling on the above $250.00; fuel, 45 days at $15.00 per day, $675.00; water 10 dollars per day, 45 days, $450.00; contract 3,052 feet at $3.50 per foot, $10,682.00; five days of 24 hours each day work, $90.00 per day, $450.00; miscellaneous tanks, pipe and fittings and supplies, $600.00; well connections $425.00; fence $58.00; miscellaneous labor and teaming $600.00; overhead $150.00; a total of $30,038.50. From that, salvage rig only, $2,437.50; miscellaneous pipe and fittings $300.00; total salvage $2,737.50; net $27,301.00.

"That he has also made calculations of drilling of the same well equipped the same way and drilled with rotary, which is as follows:

"Rig material $3,500.00; pond, labor and trucking $1,050.00; casing 260 feet 12½ inch, $650.00; 2,400 feet 8¼ inch, $3,600.00; hauling on the above $150.00, on the above casing only, fuel 25 days at $30.00 per day, $750.00, five days at $15.00, another additional fuel item, five days at $15.00 a day, $75.00; water 25 days at $50.00, $1,250.00; additional five days of water at $15.00 per day, $75.00; contract 3,052 feet at $4.25 a foot, $12,791.00; 5 days at $90.00 [fol. 459] per day day work $450.00; miscellaneous tank fittings and supplies, $700.00, well connections $425.00; fence $58.00; cement and cementing $500.00; miscellaneous labor $350.00; overhead $150.00; total $26,704.00; salvage, rig material $2,625.00; on that item miscellaneous fittings, tanks, and supplies, $300.00; total salvage $2,925.00; making net $23,779.00.

"The cost of the above well, standard tools, is a net figure of $27,301.00, with rotary tools $23,779.00. The above cost is a fair and reasonable cost of these wells drilled in September of last year, and, in my opinion, could be drilled for that cost.

"That if he had as many as twenty wells to drill in Carson County, it could be done pretty close to 5% cheaper on the cost of the well.

"The figures on Fuqua No. 2 of Black & Veatch, the Cities Service and Richie are as follows:

"Black and Veatch cost $19,843.00, Hamilton cost $24,991.00, Richie's cost on standard tools $22,302.50, with rotary $22,100.50; Burnett No. 14, actual cost of the well as claimed by Cities Service, $30,197.13, Burnett No. 14, Black and Veatch cost $30,024.00, Hamilton cost $32,847.00, Richie, standard tools $27,301.00, with the rotary $23,779.00, the actual cost as shown by the exhibit $35,624.29.

"That the cost of drilling gas wells in the Amarillo field in September, 1931, was less than it was in 1928 and 1929."

The witness, Richie, testified on cross-examination that in making his estimates he used casing and tubing and not line pipe.

In calculating the price of new materials, it is calculated on the price at the local supply house and not at the mills.

Frequently, the estimated price of the cost of building a well varies several thousand dollars on the completed well. [fol. 460] If the cost of a well exceeded the estimate made, I would say there were some contingencies that I had not taken into consideration.

On redirect examination, the witness stated that he deemed the estimate made by him sufficiently high to take care of the average contingencies.

That he is in the contracting business and would be willing to drill the wells at the prices above testified to and to make it a turn-key job. That sometimes a well costs less than the estimate.

On re-cross examination, he stated he had provided for contractor's profit in the estimate made in the item of 2,736 feet at $3.50 per foot. General experience has taught him to make his bids a little bit over his estimate. That his estimate is a little bit high in this case. If this well did cost $30,000.00, he would still say that his judgment was probably right and that the employes did not follow instructions.

[fol. 461] Account No. 1314. Production—Field-line equipment:

It was agreed by the parties before the District Court that:

"This account covers the labor and material necessary to construct and test pipe lines between the wells and transmission system. The account is valued by Black at $3,548,102.00 new and $3,126,159.00 depreciated. Hamilton valued the account at $4,447,806.00 new and $4,169,763.00 depreciated, the difference between the two engineers being $899,704.00 new and $1,043,604.00 depreciated.

"In pricing this account, Black testified that all field lines in Texas up to and including 4-inch were priced on the assumption that they were buried at one-half the depth of the main line and that in other states field lines up to and including 12¾ inch were assumed as being placed in trenches one-half the depth of the main line of the same size, and that ditching and backfilling was included on the basis of half depth on all lines in consideration of the fact

that approximately 872,000 feet of field lines are above the ground."

"Eastman testified that in his valuation of this account field lines above ground and those buried were separated, and the unit costs applicable were used.

"The commission found the value of this account to be $3,126,159.00, being the exact figure testified to by Black.

"The commission stated in its opinion that any necessary adjustments as to cost of pipe would be considered in connection with Account No. 1333, and such adjustment was made by adding to Account No. 1333, the amount of $544,552.00, plus $19,059.00 for overheads, for pipe in Accounts 1314 and 1333. An additional amount of $82,976.00 for pipe paint was added in Account 1333, making the total of that Account, new, including additions for pipe in Account 1314, $43,746,298.00, as noted in the opinion."

[fol. 462] Black testified for the Commission that in the Texas field he applied one-half the depth of the main line to the gathering lines, four inches and under in size. All sizes above that were taken at the same depth as lines anywhere in the main system, and have applied no place in the system half the depth to the field line greater than 10¾-inch. So far as the Texas field is concerned, the amount allowed for installation is exactly the same as we have allowed anywhere on the main line system. Half the depth of the main line was applied in Texas on 4-inch pipe or smaller. To the field lines in other states we have used half the depth of main lines up to 10¾ outside diameter. We have not figured a 16-inch pipe line in half the depth of the main line ditch, but have given it full depth. My exhibit shows some 3-inch line with 24-inch cover, also some with 22-inch cover, 4-inch line with 15-inch cover, some with 24-inch, 26-inch, 20-inch and some with 18-inch cover; that he used the same depth of ditch in the Texas field as was used by the company's engineers; that fifty per cent of the main line cost was applied only to the small size of pipe in Texas; that is partly an assumption and partly because of the fact that in this system in field lines, maybe some main lines, we have approximately 900,000 feet of pipe above ground to which we have given the depth of the ditch, cover, and et cetra; that applied in that particular classification he thinks that the fifty per cent allowance is absolutely fair and perhaps in excess of the actual conditions if thorough

inspections were made of the depth of those lines; I have covered a good many of the lines in Texas and it is all a matter of whether it averages or not by any system of inspection. It depends on whether you make enough inspections to make the average. Those costs of field line trenches are figured as having been dug with a ditching machine. I am referring to one half of the excavation and one half of the back filling which is only a certain per cent of the entire cost of laying the line. I do not mean that we [fol. 463] actually complete the operations of pipe laying, ditching and backfilling, at extra for half the price on a 4 inch field line, that we do on a 4 inch main line. Our fifty per cent figure is only on the item of excavation and back filling. For example on a 4½ inch, 10.79 lb pipe of which we have some in the Amarillo field, the unit cost of that pipe complete, that is, the labor in the main line would be $0.0316 and on a field line would be 29¢, or there is a difference of 3 cents per foot, or ten per cent.

I have my breakdown from my unit cost of ditching as follows:

One foreman at $7.00, one gang mechanic at $6.00, one timekeeper at $5.00, sixteen laborers at $3.20, or a total of $81.20, one medium sized truck and driver at $25.00, two light automobiles at $6.00 each, three teams with drivers at $6.00 each, two ditching machines with operators at $30.00 each, or a total of $224.20, plus 22% structural overhead or $49.32, or a total of $273.52, plus an allowance of $10.00 for planking and bridging material, or a total of $283.52 for a day's run of the gang of 850 yards, or a cost price of $0.333 per yard, and I have used $0.35.

On backfilling, I used one foreman at $4.50, one backfiller operator's helper $4.50, eight laborers at $3.20 each, one backfiller and operator at $22.50, or a total of $57.10. Add structural overhead of 22% or $12.56 making a total of $69.66 for a day in which this crew handled 900 cubic yards at a cost of $0.0774 for which I used $0.08.

In figuring structural overhead, I have considered the variation in workmen's compensation and public liability rates in the various states and have arrived at totals for said overheads as follows:

Texas, 23.46%; Oklahoma, 19.914%; Nebraska, 21.894%; Missouri, 21.414%; Kansas, 19.330%, and have arrived at the average figure of 22%.

[fol. 464] For the unit cost on labor on plain end 12¾ inch pipe, I have one foreman at $9.00, one at $8.00, one at $6.00, pipe stabber at $8.00, gang mechanic at $6.00, forty laborers at $128.00, timekeeper at $5.00, heavy truck and driver at $15.00, two light automobiles at $44.00, three teams and drivers at $18.00, one tractor and operator at $17.50, or a total of $264.50, to which has been added structural overhead in the amount of $58.19, making a total of $322.69. The percentage of overhead was 22%.

Eastman testified that in valuing this account an inventory was made of all field lines showing those above ground and those buried, and as to those buried the depth of the trench. This inventory shows that 12% of the field lines were above ground and 88% buried.

Eastman further testified that the unit costs used in the valuation of this account were prepared from studies made of the actual experience of the Cities Service Gas Company in constructing field lines utilizing 20,000 tons of pipe.

A. D. Bechtel, testified for the Company in substance as follows:

I live in Oakland, California, and am President of the Bechtel Kaiser Company, Ltd., Vice President of W. A. Bechtel Company, member of the executive committee of Six Companies, Inc., Vice President of Bechtel, Kaiser Rock Company, director of Bechtel Kaiser Warren Company, and partner in Bechtel Brothers. Bechtel, Kaiser, Ltd. is the only one of the above companies that does pipe line construction. They have been in the business about three years and in the last three years have built 65 miles of 20, 16 and 12 inch for the Montana Power Company, 200 miles of 18, 16 and 12¾ inch, 8, 6 and 4 inch for the Western Gas Company, 110 miles for the Texhoma Natural Gas Company of 24 and 12 inch, 140 miles for the Panhandle Construction Corporation 24 and 12 inch, 60 miles for the Stumpne Company 20 and 26 inch, 56 miles for the Pacific Coast Electric Company of 20 inch. My bids on these jobs [fol. 465] did not include materials that became an integral part of the line. Just such materials, supplies and equipment as was necessary to construction or laying the line.

I allowed in those contracts from 15 to 30 percent for contractor's profit depending on the size and type of line. I never allowed as low as 10% and am of the opinion that I could not stay in business in competitive bidding on 10% profit. There is no definite graduation in the percentage of profit. It depends on the size and type of line, involving different degrees of management, allocation of management time, etc.

I am familiar with field lines in connection with a gas system as distinguished from main transportation lines. I would say that the laying of a field line would cost more than to lay a main line.

On cross examination the witness, Bechtel, further testified:

"Q. I would like to know what you had in mind when you said it cost more to lay a field line?

A. I had in mind the particular contract we had, a given contract for the Texhoma Natural Gas Company which constituted approximately 110 miles of 12¾ and 24 inch, in Texas, which constituted the stem across the what might be termed the foot of the Panhandle line, Texas to Chicago."

It would probably be termed a trunk line. That is the only definite contract we have had that might be definitely called that.

From my experience in the one contract, the Texhoma line, I am of the opinion it costs more to lay a field line than a main line of the same size. From my observation, it is my personal opinion that field lines as shown by that contract contain more side or smaller connections coming into it, also considerable additional percentage or volume per mile of drips and other appurtenances which interfere with the cost. Also that usually the quantities which are [fol. 466] involved are smaller than on a main line job. (Tr. 2280.) In other words, it is the drips, fittings, connections and other appurtenances that make the differences, which are more than on a main line. In addition to the extra appurtenances above enumerated, there should be added the extra time it takes to do the work by the gang in attaching them.

E. McDonald Biddison testified for the Company as follows:

That he had been connected with the management both during construction and operation of gas concerns both in the Midcontinent field, Pennsylvania, West Virginia and Ohio over a period of 25 years, and has layed both main and field lines.

I call a field line a gathering line or a gathering line a field line, the connection from the wells to a central point in the field. The field line would usually cost more than for the same length and size of main line because of a greater difference in construction due to obstructions, usually less advantageous territory in which to lay the lines, cross connections to be made, further more in the construction of field lines, usually short sections are laid at a time. The expense of an organization moving into these short jobs is about the same as the expense would be to move a gang in to do a long job. Often the jobs are too short to justify the bringing of a ditching machine. In fact, field lines seldom justify the use of a ditching machine up to a pipe over 10 inches in diameter. My connection with such lines has been that of supervising, designing and inspecting, have also had charge of operation of pipe lines.

The witness, Biddison, further testified on cross examination that there is no maximum size of line that would be classified as a field line or a main line, but it depends upon the purpose to which it is put. There could be a 24 inch field line. Field lines are generally smaller. However, in some fields they may be as large as the main line. Gen- [fol. 407] erally, field lines are buried as deep as main lines and I have seen some gathering lines layed on top of the ground. The Cities Service Company have some, have seen them quite often. If layed on top of the ground, they would not be as expensive as if they are buried in a ditch or trench.

T. R. Jones, of Dallas, Texas, testified for the company as follows:

That he was a pipeline contractor connected with the Oklahoma Contracting Company, a corporation, and is president of the same; been engaged in the pipeline contracting business for fourteen years, during that time has layed

9,000 miles of pipeline; in the year 1930 layed a double ten inch line from Jenks, Oklahoma to St. Louis, Missouri for the Ajax Pipe Line Company. The length of it was 400 miles. Also layed a 22 inch line for the Southern Natural Gas Company in Mississippi and Alabama, the length being approximately 300 miles. In the year 1929, also laid several thousand miles of the Lone Star Natural Gas Company line of all sizes from 4 inch up to 20 inch; have also laid several lines for the Cities Service Gas Company, being some of the lines involves in this controversy, such as the 20 inch line from Wichita to Ottawa, Kansas; have laid about 100 miles of the Continental 24 inch line from Texas to Chicago. The aggregate amount of money involved in the above contracts was around $20,000,000.00, that is, for labor; is familiar with pipe line systems generally, both as to main and field lines, most of the work being main line work, but has worked on some field and gathering lines. It costs more to lay field lines than main lines; that 20% is the amount used for contractor's profit; a job is figured by the actual labor cost multiplied by two and add 20% for profit; that usually brings it within the range of competitors. The witness Jones further testified on cross examination that, in his opinion, contractors can not operate on a 10% basis and remain in business.

[fol 468] Ross M. Stuart testified for the Company as follows:

I have had pipe line experience since 1905, am familiar with field lines as distinguished from main transportation lines, am familiar with the cost of ditching and backfilling of field lines as compared with main lines. It almost always costs more to put in a field line of a given size than a main line of the same size. Field lines are usually small jobs. In laying them it is often necessary to go around rigs, tanks, houses and camps, which makes the expense greater. Also they have more connections, taps, drips, gates and that sort of stuff in field lines than in main lines. It is generally understood in the industry that field lines cost more than main lines.

Ten to 15 per cent of the Company's field lines in Kansas and Oklahoma would be laid by ditching machines. In

Texas, perhaps 60% of the field lines would be laid by ditching machines. Ditching that is fit and proper to be done by machines is cheaper than by hand.

The witness, Stuntz, further testified on cross-examination:

Field lines are laid practically at the same depth as main lines. Some of the Company's lines are laid on top of the ground but very few are thus laid. There are some in Labette County and also in Pawnee County. It would be cheaper to lay the pipe on top of the ground.

Account No. 1325. Transmission Land:

It was agreed by the parties before the District Court that:

"Black valued this account at $149,202.00 included in which were compressor station sites at Hogshooter and Owasso valued by Black at $2,000.00 and $2,000.00 respectively. The Commission deducted both the latter amounts and found a value for the account of $145,202.00. If the Hogshooter station site should not have been eliminated [fol. 469] there should be added $2,000.00 to the value found. The stipulation as to the evidence pertaining to the Hogshooter station is condensed under Account No. 1328."

Accounts Nos. 1307 and 1327. Production Rights of Way. Transmission Rights of Way:

The following agreed statement and testimony is a condensed statement of the evidence introduced on these accounts.

"These two accounts cover rights of way for production and transmission lines and telephone lines used in connection therewith and are being considered together for the reason that some controversy has arisen as to how the respective engineers classify particular lines as between production and transmission.

"Combining the two accounts Black allowed $1,208,564.00 for both cost of reproduction new and depreciated and Hamilton allowed $3,696,804.00 for both cost of reproduction new and depreciated, the difference between the two engineers

being $2,488,240.00. The Commission allowed for both accounts $1,713,512.00 or $1,983,292.00 less than Hamilton.

"There are in the system 65,440 rods of telephone right of way which Black priced at 25 cents per rod and Hamilton at 15 cents and 20 cents per rod. There is included in Black's valuation $16,360.00 for telephone right of way and Hamilton's valuation $12,475.00.

"As to the number of rods of pipe line right of way involved in the two accounts Black testified to 1,212,251 and Hamilton testified to 1,180,102. Black computed his rodage from maps furnished by the respondents which, in error, did not show certain lines which had been reclaimed and abandoned and the rodage as testified to by Hamilton is correct.

"As to the unit cost per rod to be applied to the number of rods in the system Black testified that he had never purchased any right of way and that the figures used by him were the result of information procured by his organization from other pipe line companies operating similar lines.
[fol. 470] "Eastman, testifying as to Hamilton's valuation, testified that the figures used by him were the result of studies of the actual experience of the Cities Service Gas Company in the purchase of right of way in the territory under consideration, by studies of the experience of the Continental Construction Corporation in connection with its recently built line from the Amarillo Field to Chicago, but he furnished no data as to the experience of any of these companies.

"Black testified that the unit costs developed by him were 85c per rod on pipe lines under 16-inch and $1.20 per rod for lines of 16-inch and over, made up as follows:

Cost of right of way	50¢ per rod
Damages and fencing for lines under 16"	20¢ per rod
Damages and fencing for lines of 16" and over	45¢ per rod
Cost of securing right of way for lines under 16"	15¢ per rod
Cost of securing right of way for lines 16" and over	24¢ per rod

"Black testified that he computed the cost of securing all the right of way involved with the inclusion of an allowance for transportation, legal, and miscellaneous expenses, and arrived at a total cost of $202,000.00; that in round numbers

there were 3,000 miles of right of way which divided into the figure of $202,000.00 resulted in a figure of 21¢ per rod for cost of securing right of way; that he considered an allowance of 15¢ per rod for securing right of way on lines under 16-inch and 25¢ per rod on larger lines; that an average total cost for all right of way was $0.997 per rod.

"The witness Clinton H. Montgomery, employed by and testifying for the Commission (T. 2768), stated that he had made an audit of the books of the company covering 6,215,512 feet of pipe line and that the right of way and damage costs total $407,179.82, or an average of $1.08 per rod; that the number of rods included in his audit totaled 376,698 or 31% of the total rods included in Accounts Nos. 1307 and 1327; that 171,638 rods of said total were for lines under 16 inch and 205,060 rods for lines 16 inch and over; that applying Black's allowance of 85¢ per rod for lines under 16 inch and $1.20 for lines 16 inch and over would result in a figure of [fol. 471] $391,964.00, or $15,216.00 less than the cost of right of way and damages of $407,179.82 as found by the audit.

"In his application of unit costs Eastman divided the system of the Cities Service Gas Company into nine groups. Group 1 consisted of four counties in Texas, four counties in Oklahoma and two counties in Kansas, comprising in all 84,177.9 rods, to which he applied a unit price of $2.11 per rod; group 2 consisted of one county in Nebraska and nine counties in Kansas comprising in all 90,152.6 rods, to which he applied a unit price of $2.44; group 3 consisted of five counties in Kansas comprising in all 144,168.2 rods to which he applied a unit price of $2.86; group 4 consisted of four counties in Kansas and one in Oklahoma comprising in all 170,249.2 rods, to which he applied a unit price of $3.49 per rod; group 5 consisted of twenty-two counties in Kansas, one county in Nebraska and nine counties in Missouri comprising in all 397,423.9 rods, to which he applied a unit price of $3.54 per rod; group 6 consisted of four counties in Oklahoma, two counties in Missouri and one in Kansas comprising in all 103,430.6 rods, to which he applied a unit price of $3.02; group 7 consisted of three counties in Missouri comprising in all 17,510.0 rods, to which he applied a unit price of $2.54; group 8 consisted of eight counties in Oklahoma comprising in all 103,471.8 rods, to which he applied a unit price of $3.01 per rod; group 9 consisted of six counties in

Oklahoma comprising in all 69,517.4 rods, to which he applied a unit price of $2.95 per rod.

Eastman testified the breakdown of the unit price of $3.54 applied to group 5, the largest one of the groups, was as follows:

Aerial surveys	$0.10 per rd.
Field surveys in staking the route of the line	.19 per rd.
Right of way payments for purchases of easements from land owners	1.25 per rd.
Crop damage and damage to fences and trees	.70 per rd.
Expense of obtaining right of way agreements	.30 per rd.
Abstract and recording of right of way agreements	.10 per rd.
Miscellaneous expenses	.10 per rd.
Clearing, grading and fencing	.80 per rd.
	$3.54 per rd.

[fol. 472] W. S. Gibson, called as a witness for respondents, testified (T. 2192-2196) that he was associated with the Prairie Pipe Line Company and had been since its organization twenty-two or twenty-three years ago, which, prior to 1915, was the Prairie Oil & Gas Company; that he has procured rights of way for that company for the past twenty-two years; that his experience has been in Arkansas, Texas, Oklahoma, Kansas, Missouri, Iowa, Illinois and Indiana; that during the time he has been associated with that company there has been purchased, under his direction, in excess of 10,000 miles of right of way; that he has been furnished with the cost analysis covering right of way used by the engineers for the respondents; that his experience has been on the basis of 8-inch lines and that he is not familiar with 16 inch or 20 inch lines; that right of way for lines in excess of 8 inch would cost more than for an 8 inch line; that on the basis of eight inch lines the cost analysis furnished by respondents appears to be about 37¢ a rod more than his experience; that included in the cost analysis furnished are two items with which he is not familiar, one being grading right of way, which, in the practice of his company, is handled under construction; that if there is eliminated from the unit cost analysis used by respondents' engineers the item of clearing and grading and

the item of aerial survey, the remaining figures are approximately correct:

"Q. In the figures used by Mr. Black he has used as the total of all items entering into right of way the sum of 85 cents for pipe 12 inch and under and $1.20 for pipe over 12 inch and up to 24. How do these figures correspond with your experience?

"A. That includes right of way damages and acquisition?

"Q. Yes, sir, right of way damages, acquisition and cost of acquiring.

"A. Well, acquisition is cost of acquiring. Why, that cannot be done. You cannot acquire it for that" (T. 2186-2187).

"B. H. Hicks, of Wichita, Kansas, testified for respondents (T. 2313-2330) that he was employed by the Cities Service Gas Company, his duties being buying pipe line right of way and settling damage claims; that he has had [fol. 4731] about four years' experience in that business; that from his experience it costs his company approximately $1.00 a rod as payment to the land owner without consideration of other elements of cost; that it is his practice in starting out to try to buy right of way for 50¢ a rod and if a farmer is encountered who will not accept 50¢ to pass him by and later come back to him; that perhaps they will have to pay such a man $230 for right of way and damages lumped together; that it is the practice and his instructions to settle all damage in advance, if possible at 50¢ per rod; that what he tries to do is purchase right of way at 50¢ per rod and settle damages for 50¢ a rod; that to start with a farmer is offered 50¢ a rod for right of way and 50¢ a rod for damages; that this is true in both Kansas and Missouri; that the average for damages per rod is about 65¢; that in states in which the Cities Service Gas Company's lines are located the average cost of acquiring right of way is 22¢; that if the owners of property are no more than 400 miles away they are interviewed personally; if they are in foreign countries negotiations are made by cable or wire; that a notary is carried along with right of way parties to take acknowledgements and is paid by the day; that the witness has nothing to do with such matters after the right of way contract is mailed to the home office and has no acquaintance with subsequent costs.

B. H. Hicks, testified:

"Q. Take the system as a whole with an average of pipe composing the main transportation lines, what has been your experience as to the cost per rod of obtaining right of way? I mean, what is your average—I will make it a little different. Divide it up. What do you have to pay a landowner on an average for right of way as of September 1, 1931?

"Q. Do you offer them 50 cents to start with for right of way and 50 cents for damages?

"A. Yes.

"Q. In what states is that true or prevalent?

"A. In Kansas, Oklahoma, Texas, Missouri and Nebraska.

"Q. There is no difference between the different states; you offer them 50 cents for right of way and 50 cents for damages the same as in Kansas and Missouri, to start out with?

"A. Yes, sir."

[fol. 474] "Q. What, in your opinion, on an average, does it cost in the states in which the Cities Service Gas Company line is located, to acquire your right of way?

"A. I would say 22 cents a rod would be very conservative."

"Q. This price you have just given, as I understand, is the same for the various states where you have purchased right of way?

"A. Practically so, yes.

"Q. What states are those?

"A. Texas, Kansas, Oklahoma, Missouri and Nebraska.

"Q. Do you find any difference in any of the states as to what these costs are, what you have stated here would be the cost in each one of the states?

"A. About a general average; yes, sir.

"Q. And be about the same in one state as it would in another?

"A. Practically."

"The Commission used the figure of $1.40 per rod which it arrived at by taking the actual average cost of right of way and damages of $1.08, as shown by the books of the

company according to an audit made by C. H. Montgomery, and adding thereto 22¢ per rod for expense of acquisition and 10¢ per rod for expense of abstracting and recording on other than telephone rights of way and allowed for the two accounts $1,713,512.00, which is an increase of $504,948.00 over the estimate made by Black but $1,983,292.00 less than the estimate of Hamilton.

"The Commission applied to the rodage in the system a price of $1.40 per rod arrived at by adopting the figure of $1.08 per rod, testified to by Montgomery in connection with his Exhibit 87, as representing the cost of right of way to the company and added thereto 22¢ per rod for expense of acquisition and 10¢ per rod for expense of abstracting and recording.

"EASTMAN testified that Montgomery's Exhibit 87 did not represent the total cost to the company, his testimony in that regard being as follows:

"In regard to right-of-way, Mr. Eastman, as I recall the testimony, Mr. Montgomery made some studies or checked some information from the books of the company which were given to Mr. Black and used by him in figuring the unit cost which he arrived at. Do you know what those records consisted of?

"A. I presume they consisted of the job order analysis of the various lines.

[fol. 475] Mr. Welch: Do you know, Mr. Eastman?

A. Yes, sir, I do know.

Q. Do these job orders contain all of the costs, not included (included in) right-of-way?

A. No, sir, they do not.

Q. What elements are not included on the job orders?

A. The entire cost of acquiring the right-of-way, cost of abstracting, recording and a considerable portion of the right-of-way payments and damages payments are not included in this job order analysis as right of way costs.

Q. So if it should be assumed that those job order contained all the costs in connection with right-of-way, his assumption would not be correct?

A. That is not correct, no, sir.

Q. And of course, would be insufficient?

A. May I further explain why it is not correct?

Q. Certainly.

A. The work of obtaining right-of-way is carried on by the land and lease department of the several companies operated from the Bartlesville office. The salaries and expenses of these men are charged to operating expenses of the land and lease department. No attempt is made to classify these expenses by the various lines. At the end of each month, the proper portion of the expenses of this department is capitalized in a lump sum and goes into the investment records of the company as a lump sum. A considerable portion of the cost of settling damage claims and damages, for abstracting and recording, is done by the legal department. At the end of each month a proper portion of this expense of the legal department is capitalized in one lump sum, therefore, it is not possible to go back to the individual job orders and obtain all of the right-of-way costs.

Q. You would have to go to many different sources in the office to determine what these costs actually are?

A. You do, yes, sir.

Q. And did you go through all of the sources of information that you know of in arriving at the figure which you used?

A. We did • • •.

Q. I will ask you to look at Exhibit 87 just introduced by Mr. Montgomery in regard to the cost of right of way; I will ask you to state whether the cost shown on that exhibit and stated to be obtained from job orders is the entire cost in connection with that item.

A. The costs of right of way as shown on Exhibit No. 87 are not the entire costs of right of way on the various lines. As I explained some few days ago at a previous hearing, these costs include nothing for the acquisition of the right of way, which is a major item.

Q. What do you mean by cost of acquisition of right of way?

A. Going out and securing right of way, having it abstracted and recorded.

Q. That is, it does not include the expense of men in the field, the automobiles, phone calls, and all that?

A. No, sir, it does not.

[fol. 476] Q. And that, you mean, is the major item in connection with procuring right or way?

A. That is a major item.

Q. Where do those costs appear?

A. They appear eventually in the plant and investment account of the company as overhead construction costs capitalized, or I believe the caption here as shown in Mr. Montgomery's Exhibit No. 91, is 'General Construction and Investment Expenditures.' They are not reflected by individual job orders.

Q. So Exhibit 87 does not include all the costs of acquiring right of way?

A. No, sir, it does not.

Q. Have you considered all of thes matters in the unit costs you have used?

A. We have, yes.

Q. And did you arrive at these costs by studying the actual experience of the company?

A. We did, I might further say that these costs as shown in Exhibit 87 include nothing for locating right of way originally. The cost of that also enters the investment account of the company through General Construction and Investment Expenses. * * *"

"On cross-examination Mr. Eastman testified as follows:

'Q. It is possible that in this job account for the Cities Service Gas Company that the legal expense and the expense of obtaining the abstract and incidental expenses of the right of way, etc., are included right in that job account, isn't it?

'A. From the way in which this sheet is prepared it is possible, for from my knowledge of actual practice of the company I would say it does not include any of these items.

'Q. It is not true, then that always on a job order with reference to construction of pipe lines the legal expense, including expense accounts and incidental expense, telephone, etc., are carried in some other account; but it is possible they may be carried in the job account; is that right?

'A. It is possible they might be carried in the job order, yes, sir'' (Tr. 2797, 2789).

"Black has included engineering and staking out under the engineering account, No. 1390. The cost of clearing,

grading and construction damages have been included under construction cost. These items appear to be properly included in these accounts under the practice of the company. Exhibit 38 consists of one of the contracts under which the contractor agrees to perform the following services:

'It is mutually understood and agreed between the parties hereto that the prices thereinabove mentioned and set forth to be paid second party by first party includes the costs of clearing the right of way before construction and cleaning up right of way after the completion of the work and shall also cover all repairs to fences and all *all* costs [fol. 477] of other improvement damages which are to be paid by the second party hereto free of any cost, charge or expense to first party.

'Such damages for which the contractor is responsible includes repairs to fences, hedges and roads, and damage done to or by stock escaping through fences or gates left open or insecurely closed, as well as any and all damage to stock on account of being frightened, damage due to cutting hedge, damages to travelers in horse-drawn or automobive equipment, or stock caused by open ditches, and in general any damages that might have been avoided by care on the part of the contractor. All such claims for damages for which the contractor is liable shall be settled by the contractor' (Ex. 38).

"This contract also provides that the contractor is to receive construction material furnished by the company at rail points closest the work and to transport such material used in excavation and construction of the pipe line and back fill for certain stipulated prices. Grading of the rights of way, which is a construction cost, is not mentioned in the items which the company is to furnish or perform for the contractor, and is included as an item incidental to excavation.

"BLACK testified as to serial survey as follows (TR. 2063).

'Q. Aren't all the pipe lines being built now first surveyed with an aerial map?

'A. I don't think these lines were or are.

'Q. You have thrown out any aerial map because it was not used when the lines were constructed. I don't see

why you should do that and put in a ditching machine when that did not exist?

'A. I would be quite willing to include the cost of an aerial survey for the main lines of this or any other system, if the system reflects the advantages we would get from such a survey.

'Q. Well, if this system were to be built to-day, and none of it existed at all, wouldn't you start in with an aerial map?

'A. I might, but the valuation of this particular system is of this system as it now is, and the chief advantage of an aerial map is to show you how you can better your location or speed up the construction, or do a thousand and one things which have not been done in this property as it now exists.

'Q. But if we are reproducting it now, to-day, on which the theory of the valuation is, we would start in with an aerial map, wouldn't we?

'A. If you were reproducing it to-day I don't think you would build the property in the same location. You must remember that the valuation we are making is of this property in a specific location.' ''

[fol. 478] Account No. 1328. Transmission—Compressor station structures:

The evidence pertaining to this account was submitted to the District Court on the following agreed statement and evidence:

''This account includes buildings, housing compressor stations together with dwellings, garages, machine shops, dams and other buildings used in connection therewith. It does not include the equipment or furnishings in any of these buildings.

''This account was valued by Black at $1,806,823.00 new and $1,567,605.00 depreciated. It was valued by Hamilton at $2,482,629.00 new and $2,267,443.00 depreciated. The difference between the two engineers on depreciated or present value is $699,838.00.

''The Commission found the present or depreciated value of this account to be $1,466,102.00. The difference between

the value found by Hamilton and the value found by the Commission is $801,341.00.

"Included in this account at the compressor stations at Hogshooter, Hominy and Owasso, Oklahoma, and the present value of the structures as found by Black and by Hamilton in the following tabulation:

Structures	Black	Hamilton
Hogshooter Station	$49,560	$84,999
Hominy Station	7,793	8,897
Owasso Station	44,150	55,683
Total	101,503	149,779

[fol. 479] "In arriving at its value of $1,466,102.00 the Commission accepted the present value as testified to by Black and eliminated the present value of the structures at Hogshooter, Hominy and Owasso as testified to by Black in the total sum of $101,503.00. The difference between Black and Hamilton of $699,838.00, when added to the $101,503.00 disallowed for the structures at Hogshooter, Hominy, and Owasso, makes the total of $601,341.00, which is the difference between the valuation testified to by Hamilton and the value found by the Commission.

"Black introduced in evidence, as Exhibit 53, photostatic copies of sworn tax returns of the Cities Service Gas Company to the Oklahoma Tax Commission in which reports it was stated that at the date of said returns, February 1, 1931, the Hominy compressor station was being reclaimed and that the Hogshooter compressor station 'is now and has been abandoned for several years. This property is now subject to sale and reclaim and has only a junk or salvage value of not to exceed $5,000.00.'

"It is admitted that the Owasso station is not connected with any lines of the Cities Service Gas Company; that the equipment has been moved from the station and that the station is not used or useful at this time in gas operations.

"Eastman testified that the Hogshooter station was originally constructed to pump gas out of the Hogshooter Field into the Kansas Natural system; that the Hogshooter Field became exhausted and lines were extended to the South into the Owasso and Catoosa districts and the station became a main line station boosting gas from the

South and also pumping gas from the field to the west; at that time the load on the system had not assumed anything like present proportions and when the fields to the South became exhausted the Hogshooter station was used to pump gas from the Osage Fields North through the Kansas Natural System; during the last three, four or probably five years, the station had not been operated due to the fact that additional compressor station capacity was installed at the Tallant station and the main source of gas [fol. 480] supply shifted to other locations; that the lines to the Hogshooter station are coupled with old styled dresser couplings not capable of standing the high pressures under which the company now operates; that for three or four years it was thought probable the Hogshooter station would be abandoned and reclaimed and it was the intention of the company to so abandon and reclaim it but this was not done; within the last year one of the major sources of supply for the system has shifted to the Oklahoma City Field, which makes necessary a complete rearrangement of operating conditions; that the discovery of gas in the Oklahoma City Field has necessitated a complete rearrangement of operating conditions; that in order to render service on the eastern portion of the system it is now necessary to either increase the compressor station capacity at Tallant or operate the Hogshooter station; that it will probably be necessary to construct a line from the Oklahoma City Field in an easterly direction to connect with the Seminole line if the company is able to maintain a supply of gas. The Company is only refraining from operating the Hogshooter station at the present time because of the fact that before it is placed in operation, except in case of emergency, it is the desire to weld the 18-inch line extending North from the station so it will be capable of carrying high pressures; and that a requisition for that work has been prepared at the present time.

Eastman testified on direct:

'Q. In your opinion, Mr. Eastman, is that Hogshooter station at this time useful to the pipe line project of the Cities Service Gas Company?

'A. Yes, sir, it is.

'Q. And it is the bona fide intention of the company to place it in operation?

'A. That is correct. I am not positive that it is in operation today? (Tr. 2523-2529)'

[fol. 481] "On cross-examination by attorney for the Commission Eastman testified that the Hogshooter station was constructed about 1909; that an 18-inch line leads North from the station and a 16-inch line West. The station was shut down about 1924 or 1925 and has not been in active operation since that time; since that time the station has not been used for the purpose of supplying gas to the customers; the total value placed on the station by Hamilton and the Witness was $756,682.00 new and $426,792.00 depreciated; that land valued at $2,000.00 is not included in the figures given; that the figures given do not include undistributed overheads.

"As to Hominy, Eastman testified that the compressor station had been removed and that all that remained and all included in Hamilton's valuation were several cottages used by the pipe line employees, the rental of which is included in the exhibit covering income and a water pump and gas engine, the use of which the witness did not know unless it was fire protection for the cottages, but that if the pump and engine were not used and useful they would have been reclaimed.

"W. D. Truman Construction Engineer for the Kansas City Structural Steel Company, testified that he was employed by the respondents to estimate the cost of the main structures at the five compressor stations located at Higgins, Texas, Tallant and Drumright, Oklahoma, and Ottawa and Graham, Kansas; that he was familiar with the construction of structural steel buildings but not concrete foundations; that he selected George P. Reintjes, a contractor of Kansas City, Missouri, to estimate that part of the work for him; that Truman visited all compressor stations and Reintjes visited all but Higgins, and estimated in detail the cost of their reconstruction; that their estimate of the various stations, as compared with the valuation of Black, was as follows:

[fol. 482]

Station	Black's valuation	Truman's valuation including Reintjes' estimates
Higgins	$38,010.00	$64,115.00
Tallant	26,953.00	43,885.56
Drumright	23,610.00	46,679.98
Ottawa	40,232.00	52,677.49
Grabham	51,601.00	77,197.00
	$180,406.00	$284,555.03

"Truman further testified that he added to his figures for superstructures the figure given him by Reintjes for substructures to arrive at the total given in the above table.

"The total estimate of Truman and Reintjes divided as to the part estimated by Truman and the part estimated by Reintjes, and a comparison of Truman's and Black's estimates of superstructures for the five stations is as follows:

Station	Truman's valuation including Reintjes' estimates	Reintjes' estimate of foundations, etc.	Truman's valuation of superstructures	Black's valuation of superstructures
Higgins	$64,115.00	$45,400.00	$18,715.00	$18,530.11
Tallant	43,885.56	29,403.56	14,482.00	13,020.04
Drumright	46,679.98	36,313.58	10,366.40	10,858.00
Ottawa	52,677.49	34,924.09	17,753.40	17,784.32
Grabham	77,197.00	49,410.36	27,786.64	24,502.00
	284,555.03	195,451.59	89,103.44	84,694.47

"George P. Reintjes testified for respondents that he had many years' experience in the construction business and that his estimate for the foundations and substructures of the five compressor stations was correct.

"George Rinner, an experienced estimator for the Leeper Construction Company of Topeka, Kansas, testified that he had been employed by the State to estimate the foundations and substructures at the Ottawa and Grabham compressor stations estimated by Reintjes and that his estimate for the construction at Grabham was $28,434.00 as against the estimate of $45,019.00 by Reintjes and that his estimate at Ottawa was $19,048.00 as against Reintjes' estimate of $29,617.00 and that he would be willing to contract the work for 10% less than his estimates; that he had examined [fol. 483] Reintjes' quantities and prices on those stations, but had not estimated in detail, and the same proportionate difference between the Reintjes' estimates and his

own would apply to the five stations. The total of Rinner's estimate on Ottawa and Grabham was $47,482, and deducting ten per cent would be $42,734; Reintjes' estimate on the same items was $74,636 or 175 per cent of Rinner's estimate.

Rinner testified that his firm bid $12.63 per cubic yard of concrete, including reinforcing, forms contractor's profit, and all incidental items on the post office building at Topeka, and that his firm lost the work because it was not the low bidder.

Black made an analysis of Reintjes' figure on concrete construction on five stations, and stated that they averaged $29.69 per cubic yard at Ottawa, $41.03 per cubic yard at Higgins, Texas, $21.75 per cubic yard at Grabham, $19.91 at Drumright and $28.34 per cubic yard at Tallant; that on work designated in Black's office, Reintjes had made bids on concrete as follows: $13.40 per cubic yard on reinforced concrete at Evansville, Ind.; $21 a cubic yard on reinforced concrete at Fredonia, Kan.; $20 per cubic yard on reinforced concrete at Holton, Kans.; and that on all these jobs Reintjes was not the low bidder.

"Eastman, for respondent, testified that he had examined the records of the Cities Service Gas Company to determine the actual cost to it of the compressor station structures at nine stations and that the actual cost to the company was the figure appearing in the first column of the following tabulation, the second column of which shows the value found by Hamilton and the third column the value found by Black and that Black's figures for the nine sta- [fol. 484] tions would have to be increased 42% to equal the actual cost of the structures to the company.

Station	Actual cost	Hamilton	Black
Blackwell	$41,303	$49,401	$41,358
Corwin	58,101	57,650	34,995
Drumright	37,045	42,121	23,610
Higgins	57,658	57,650	23,610
Matfield	52,004	49,550	34,497
Moreland	64,633	59,402	39,177
Ottawa	57,726	59,402	40,232
Pampa	64,783	51,228	34,417
Wichita	84,418	72,495	77,068
Total	517,671	498,899	363,364

[fol. 485] "In explaining the figure of $77,068 found by Black for the Wichita station as compared with the figure of $72,495.00 found by Hamilton, Eastman testified:

"Q. You referred a moment ago to the comparative figures at Wichita on the compressor station. Have you those figures with the foundation included?

"A. Yes, sir; the figures which I gave applying to the main building at Wichita were as follows: Actual cost $84,418, the value which we placed on the building $72,495, and the value which Mr. Black placed on the building $77,068. The Wichita compressor station is built in a plot of low ground near the city of Wichita, and on a very sandy soil. It was necessary in the construction of that station to drive an immense quantity of piling before the foundation could be laid, and the building and the engines and everything connected with the station rests on these piling. There has been a tremendous amount of filling done to bring the ground level of the station up above the water line. In making our comparison with Mr. Black's figures, we believe that he has included certain of this piling under the engines in with the cost of the building, because the figure which we have used for the building, or the value which we have placed on the building is $72,495, and Mr. Black's figure is $77,068. The value which we have placed on the engine foundations is $73,700, and Mr. Black's figure only $36,057, making a total of the two items in our valuation of $146,193, and in Mr. Black's valuation $113,125, and the piling under the engine foundations are not reflected in the cost which I have given as the actual cost of the building. One of the exhibits that we have filed contains a very good picture of this station when it was in the process of construction, and shows the piling."

"Eastman testified that he had also made an examination of the books and records of the Cities Service Gas Company for the purpose of ascertaining the actual cost to it of the auxiliary buildings and structures on the several compressor station sites and found the total actual cost to the company of main and auxiliary structures to be as set out in the first column of the following tabulation, the second column of which tabulation shows the amount included by Hamilton and the third column the amount included by Black:

Station	Actual cost	Hamilton	Black
Corwin	$118,188 (0)	$115,763 (0)	$80,074 (0)
Higgins	129,286 (0)	122,890 (0)	89,060 (0)
Mathield	131,704 (0)	118,281 (0)	86,074 (0)
Ottawa	112,503 (0)	109,297 (0)	86,469 (0)
Blackwell	97,265 (0)	95,007 (0)	75,097 (0)
Drumright	128,320 (0)	121,000 (0)	85,874 (0)
Wichita	120,792 (0)	105,215 (0)	104,542 (0)
Moreland	132,197 (0)	119,402 (0)	85,177 (0)
Pampa	146,812 (0)	119,000 (0)	90,200 (0)
	$1,123,103 (0)	1,027,757 (0)	782,873 (0)

"Eastman testified that the figures shown in the first column of the above tabulation were accurate and represent the actual cost to the company of all buildings and [fol. 486] structures at the several compressor stations and that Black's figure would have to be increased 45% to equal such actual cost and that Hamilton's figure would have to be increased 9.4%.

"In support of Hamilton's cost of reproduction new of structures in this account, Eastman testified that no breakdown of materials and labor prices were available and produced none; Black submitted details of both labor and materials prices. On rehearing this breakdown was submitted.

"The testimony in regard to the present or depreciated condition of this account was that of Eastman, Hamilton and Black and that of P. McDonald Biddison, a gas engineer employed by respondents for that purpose. The average per cent condition testified to by the several witnesses respectively, and used by the Commission covering all the structures in the account was as follows:

Hamilton	Black	Biddison	Commission
91.33	86.76	88.82	87.89

H. D. Renfrow, superintendent of compressor stations for the company introduced an exhibit on the per cent condition of the company's compressor stations as shown by his inspection, and that he reached exactly the same per cent condition as did Biddison, to-wit: 88.82 per cent, although working independently, arrived at exactly the same figure.

"The Commission used Black's percentages as to individual structures, the percentage of 87.89 as against Black's

86.76 being the result of the elimination by the Commission of the stations at Hogshooter, Hominy and Owasso, which stations, being older, carried a lower per cent condition.

"The nine stations above tabulated were built within the past four years and represent $1,027,757.00 in value as found by Hamilton out of his total value for this item of $2,482,629.00, or 41.4%. The nine stations selected were built within the past four years and are representative of the thirty-four stations comprising the account and on this basis of original cost to the company, the total account would be $2,713,909.00 or 9% in excess of Hamilton's estimate.

"The record shows that Eastman determined the per cent condition applied to respondents property rather than applying the per cent condition found by the engineers making the inspection.

"He testified as follows:

"Q. Mr. Eastman, using the method that you have here used in arriving at depreciated condition of the production field measuring station, you are asking the present customers to give you a return upon the property at a 97 per [fol. 487] cent condition, and in addition to that, an amortization figure of, what per cent was that, eight per cent?

"A. We are asking our customers to give us a fair return on the fair value of all the property. We are also asking them to provide a revenue from which we may have our property returned to us at the expiration of its useful life.

"Q. That is, you are asking them to return the property over a basis of twenty-one years, and at the same time to give you a return upon the property value at 97 per cent of its reproduction cost new?

"A. We are asking them to provide revenues which will give us a return on the fair value of our property.

"Q. At 97 per cent?

"A. Perhaps it might clarify things slightly if I——

"Commissioner Hill: Can't you answer it yes or no?

"A. Not without an explanation.

"Q. I think my question is plain enough.

"A. Of certain property, yes, sir.

"Q. This property. We are speaking of the specific property.

"A. I would like to make a further explanation of it, if I may.

"Commissioner Hill: All right.

"A. Perhaps it would clarify the situation if I would state my position, or belief, as to what should be deducted from the rate base because of accrued depreciation or physical deterioration.

"Q. I might say this, we understand what you have done, what we are asking for now is the effect of it.

"A. I am trying to tell you the reason for it.

"Q. All right, go ahead.

"A. I believe only such amounts should be deducted from reproduction costs, new, in arriving at a rate base, as is reflected in loss, primarily, of efficient operation, or only such amounts should be deducted as will be necessary to restore the property to full operating condition. That is what we have in general done here, by rating the property in a per cent corresponding to new property and should apply to all of the property with the exception of property which it is necessary to amortize, *property which it is necessary to amortize*, in general consisting of leaseholds and wells, and other production property."

Account No. 1331. Transmission—Compressor-station equipment:

The evidence pertaining to this account was submitted to the District Court on the following agreed statement and evidence:

"This account covers all machinery and equipment used in connection with the operation of compressor stations.

"The account is valued by Black at $9,660,183.00 new and $8,482,419.0- depreciated.

"Hamilton valued the account at $9,773,788.00 new and $8,873,812.00 depreciated.

"The difference between Black and Hamilton on present or depreciated value is $391,393.00.

"The Commission found the value of the account to be $8,048,910.00.

"Black valued the equipment in the Hogshooter station at $414,925.00 depreciated and Hamilton valued the same equipment at $341,794.00.

"Black valued the equipment in the Hominy station at [fol. 488] $1,548.00 depreciated and Hamilton valued the same equipment at $1,471.00.

"Black valued the equipment at Owasso at $17,036.00 depreciated and Hamilton valued the same equipment at $14,361.00.

"On the equipment in the three stations Black was $75,943.00 higher than Hamilton on his depreciated value or 21%. The Commission eliminated from the total value of this account $433,509.00, which is Black's figure for the present value of the equipment in the Hogshooter, Hominy and Owasso stations. Hamilton's figure for the value of these stations was $75,943.00 less. but the Commission adopted Black's figure.

"If the stations at Hogshooter and Hominy should be included the Commission's value, as found for this account should be increased $416,473.00, making the total of $8,465,383.00, which is $408,429.00 less than the value as testified to by Hamilton, which is accounted for largely by the difference in per cent condition used by the respective engineers.

"No contention will be made by complainants as to this account other than that the equipment at Hogshooter and Hominy should be included in the sum of $416,473.00.

"The evidence on which these stations have been eliminated is set out under Acct. No. 1328."

Account No. 1333. Transmission-line equipment:

It was agreed by the parties before the District Court that:

"This account covers the transmission pipe line of the Cities Service Gas Company in place including both material and labor.

"The account was valued by Hamilton at $46,893,014.00 new and $43,578,602.00 depreciated. Black valued the account at $43,099,711.00 new and $38,842,371.00 depreciated. The difference between the two engineers is $3,793,303.00 new and $4,736,231.00 depreciated. The Commission valued the account depreciated at $39,432,351.00 being an increase of $589,960.00 over the value found by Black but still $4,146,271.00 less than the amount claimed by Hamilton.

"The addition of $389,960.00 made by the Commission to the value found by Black covers pipe and paint, the

[fol. 489] Commission having found the value of the pipe in the system to be $26,931,305.00 which, for the purpose of this case, will be accepted by the parties.

"The remaining difference between the value for the entire account as found by the Commission and that as claimed by Hamilton is accounted for by the difference in per cent condition found by Black and adopted by the Commission and the per cent condition claimed by Hamilton and by the difference in estimates by Black and Hamilton as to the amount of rock excavation in the system and the price to be applied to such rock excavation."

For the purpose of this appeal the parties have agreed to accept per cent condition found by the court and the unit cost which the court found should be applied to rock excavation, leaving in dispute only the amount of rock excavation to which the agreed price should be applied.

Eastman testified that the amount of rock excavation shown by Hamilton's valuation was determined by engineers sent out over all the lines for that purpose and who procured their information from surface observations and from talking with company employees who had been in charge of maintenance work for years and from repeated excavation of the lines were familiar with soil conditions. That where shoot rock was shown in the valuation it had been calculated as solid from top to bottom of the trench, and that where pick rock was shown the entire excavation had been calculated as pick rock. That he developed a unit cost of $7.38 per cubic yard for shoot rock and $4.01 per cubic yard for pick rock.

Mr. Eastman further testified:

"* * * Q. As I understand it, there is quite a difference between your valuation and Mr. Black's covering the item of rock excavation?

A. That is correct, there is a big difference.

Q. We have covered the one line from Ottawa to Wichita, which was constructed by Mr. Jones. Leaving that out, [fol. 490] what study did you make of the balance of the system to determine the percentage of rock?

A. We did not attempt to determine rock excavation on a percentage basis. At the beginning of this work, we sent four engineering parties into the field for the purpose of

checking lines. These parties were each composed of two graduate engineers, and they went over these lines in detail, in many cases walking the length of the line, together with the district superintendent of that district, or his foreman, or the line walkers. They went over each line and every line in detail to determine the amount of rock excavation on that particular line.

Q. These lines are frequently opened in maintenance work, are they not?

A. They are, and the district superintendents and operators of these lines in the various districts, have a very good knowledge of where rock exists, by the time they have lived with these pipe lines for years, as a great many of them have, quite an intimate knowledge of soil conditions and other physical conditions in the lines in their particular districts. We took advantage of all this information.

Q. And it is your belief that your figures are correct in regard to the rock that you have shown?

A. It is my belief that our figures are quite conservative as to the matter of rock.

Q. Have you made any computation of the difference in the valuations on account of rock excavation?

A. No, sir, we have not, for the reason that we have set out lines up in a different way than Mr. Black and that computation would require considerable time and amount of work to obtain. We have made comparisons on certain lines.

Q. Did you make comparisons on certain representative lines?

A. Yes, sir.

Q. What was the result of that study?

[fol. 491] A. We have made a comparison on certain representative lines between the amounts allowed by Mr. Black for classified excavation and our own allowances for pick rock and shoot rock excavation. On the Cambridge-Petrolia line, which is a 12 inch line, Mr. Black has allowed $21,043 for classified excavation. Our comparable figure is $179,986. I might further say that this line is laid almost entirely in solid rock. On the Falls City line, Mr. Black has allowed a total of $7,153 for classified exca-

vation, our comparable figure is $17,216. On the Fort Scott 8 inch line, Mr. Black has allowed $21,871 for classified excavation, our comparable figure is $67,371. On the Kansas City No. 3 line, Mr. Black has allowed $19,325 for classified excavation, our comparable figure is $24,715. On the Ottawa-Sedalia line, Mr. Black has allowed $12,757 for classified excavation, our comparable figure is $24,606. On the Topeka 16 inch line, Mr. Black has allowed $22,381 for classified excavation, our comparable figure is $63,021. On the Pampa-Wichita line, Mr. Black has allowed $13,351 for classified excavation, our comparable figure is $101,873. On the new southern trunk, 16 inch, Mr. Black has allowed $6,397 for classified excavation, our comparable figure is $15,735.

Commissioner Hill: Is that the line from Grabham east?

A. Grabham station east, yes, sir.

Commissioner Hill: How much did you allow for rock?

A. $15,735, against $6,397 allowed by Mr. Black.

Commissioner Hill: Doesn't that go straight east?

A. Yes, sir, straight east from Grabham station.

Commissioner Hill: In Labett county?

A. I am — sure whether this section of the line extends as far as Labett County or not. It is the new portion of that line. On the Wichita-Ottawa 20 inch line, which we had under discussion some days ago, Mr. Black [fol. 492] has allowed $57,155 for classified excavation, our figure, comparable to this, is $390,275. These lines are all in the State of Kansas. In explanation of the rock in the State of Kansas, I think it might be well to point the fact that there is a great deal more rock in southern Kansas than a person ordinarily thinks about. There are several limestone ridges running in an easterly and westerly direction which cross eastern Kansas and on practically each one of these ridges is located a cement plant. Our line crosses every one of these ridges and the eastern portion of the system in a country which is not normally considered as being particularly rocky, is in fact quite rocky, where our lines traverse it. On the Ottawa-Sedalia 12 inch line, in the State of Missouri, Mr. Black has allowed for classified excavation $26,080, our comparable figure is $63,962. On the Saginaw-Springfield line, Mr. Black has allowed $32,412, our comparable figure is $195,145.

Q. A number of those lines were built quite recently, were they not, within the last one or two years?

A. Yes, sir, most of those lines were.

Q. In connection with the building of those lines, I will ask you if your department had engineers present with the contractor to make time studies of the construction as it progressed?

A. We did in a large number of cases. We did not in every case, of course, but we studied quite a number of those lines during the construction period.

Q. Those men had no data other than to observe all of the different elements entering into the construction of the line?

A. That is correct, and to keep data in that connection. [fol. 493] Q. And did you consider all that information in connection with your determination of the rock formation?

A. We have data both as to determination as to the amount of rock and the cost of rock excavation. I did not cover the lines in Oklahoma and Texas, but the differentials existing in the States of Missouri and Kansas apply in a general way to our figures and Mr. Black's in Oklahoma and Texas."

Black testified with respect to classified excavation that he determined the percentage of such excavation by observation of the territory through which the major part of the line passed and from his knowledge of the territory [fol. 494] gained through more than twenty years of experience. He testified that he made a personal inspection of line "G" from Wichita to Ottawa, that he allowed $2.50 per cubic yard for all classified excavation whether solid or loose rock and had allowed this amount in addition to ordinary cost of trenching and backfilling of ditches of the same dimensions.

Black introduced exhibit 77 which compares the contract costs of unloading pipe and materials, hauling, stringing, ditching in all classes of material, laying pipe, backfilling and testing on seven of the lines in this property, with the amounts claimed in Hamilton's exhibit for "pick rock" and "shoot rock" only. Line "G" between Wichita and Ottawa, cost the company $0.59 per foot for all the above operations, including rock excavations, under a contract

dated June 22, 1928, or a total of $379,699.00. Hamilton's valuation, based on an analysis of costs of contract operations, shows the cost of rock excavation alone to be $390,276, or $10,577 more than the contract cost of all operations for the construction of this line, excepting welding and painting.

Jones testified that he was a pipeline contractor with fourteen years' experience and had constructed pipelines involving $20,000,000 for labor; that he had contracted with the company in the construction of Line "G" between Wichita and Ottawa to unload, haul, string and lay the pipe, excavate the ditches, including shoot rock and pick rock, backfill and test the line, for 59 cents per running foot. That he received a total of $895,985.67 for this contract and that he lost $128,000 on it, but he did not allocate any part of this loss to pipe unloading, hauling, stringing, ditching, backfilling, or to the other operations for which he received unit payments in addition to the 59 cents per foot, and which amounted to $516,287 in addition to the $379,699 paid for the operations included in the 59 cents per foot bid; that the reasonable cost per lineal foot for excavating solid rock would be "a little over 75 cents" in a ditch 28 inches by 40 inches; that such a ditch contains 7.8 cubic feet of excavation per lineal foot of ditch, and the cost of solid rock excavation per cubic foot may be taken as 9.62 costs. That his testimony concerning the reasonable cost for solid rock excavation was made after the completion of this contract.

Mr. Eastman testified with reference to the actual cost to [fol. 495] the company of eleven major lines which the Cities Service Gas Company had constructed during the past three or four years, the actual cost of construction was averaged as follows:

"Q. Now, you may proceed with whatever comparisons you made?

"A. We have made a comparison of eleven major lines, comparing the actual cost of labor to the company, including those lines, with the labor costs which we have used in our valuation and with the labor costs which Mr. Black has used in his valuation. These lines have all been laid within the last three or four years, and, in some cases, within the last two years. During that period of time there has been but slight decrease in any of the labor costs, so

that the figures, we feel, are fairly comparable. The lines which we have compared vary in size from 8-inch to 20-inch. In making these comparisons, it has really been necessary to make two comparisons, because of the fact that in the setup which we have used in presenting our valuation we have included the labor of placing the couplings, together with the cost of couplings. The first line on which we have a comparison was the line known as the Hutchinson-Lyons-Superior line, extending from Hutchinson, Kansas, to Superior, Nebraska, the total cost of labor on that line, as paid by the company, was $355,893. The labor cost which we have used in our valuation is $382,744. Adding now the couplings and the labor of placing the couplings, to make the figure comparable to Mr. Black's figure, the figure which we have used becomes $429,343, as compared to Mr. Black's figure of $348,436, or a difference of some $80,000.

"Q. Now that is, comparing your valuation, these several figures with the actual experience of the company and the actual cost to it in money?

"A. That is correct. In the case of the Fort Scott line, which is a line extending from a point north of Chanute, Kansas, in an easterly direction to Fort Scott, the actual cost of the line to the company,—8-inch line—was $202,184, and it should be borne in mind these costs I am quoting are for labor only, they include no material; Hamilton's estimate for labor comparable with this is $180,961.

"Q. What is the difference between the two?

"A. Approximately $22,000—$21,000.

"Q. So your figure is $21,000 or $22,000 less than it actually cost the company?

"A. That is correct. If we add to our figure the couplings to make it comparable with Mr. Black's, our figure becomes $194,736, which compares with Mr. Black's figure of $139,639.

"Q. What is the difference there?

"A. Approximately $54,000.

"Q. So it is that much less on that line under the actual experience of the company?

"A. That is correct.

"Q. Any other lines?

"A. I have eleven of these lines analyzed, I do not know whether you desire to read all of them or not. I have not had them made up in the form of an exhibit.

"Q. Well, are they all in the record, then?

"A. In the case of the Saginaw-Springfield line, which is a line extending from a point south of Joplin, Mo., to Springfield, Mo., 10-inch line, the actual cost to the company was $380,394. Our comparable figure to this is $442,570, adding the couplings our figure becomes $489,809, as compared to Mr. Black's figure of $343,085.

"Q. What is the difference on that line?

"A. About $140,000.

"Q. That is, Mr. Black is $140,000 less than the actual cost to the company?

"A. No, not less than the actual cost to the company in this particular line, less than our figure, that is $40,000 in- [fol. 496] cluding the couplings, less than the actual cost to the company, in which figures, of course, referring to the actual cost to the company of couplings or welds, are not included.

"Q. You were high on that—on your estimate on that particular line?

"A. Yes, sir, we were high as compared to the cost to the company, I am not certain as to whether we were high as to the actual cost of the line.

"Q. That depends on whether the contractor lost money or whether he did not?

"A. That is right. In the case of the St. Joseph 12-inch line the cost to the company was $144,683. Our labor figure on that line comparable to this, is $164,621.

"Q. You were low on that one—are you high or low on that?"

"A. We are high.

"Q. By how much?

"A. By $20,000. Adding the couplings, our figure becomes $190,224, which is the comparable figure with Mr. Black's figure of $157,268.

"Q. Do you know what the experience of the contractor was on that line?

"A. On the St. Joseph line?

"Q. Yes.

"A. No, sir; I do not.

"Q. The next line?

"A. In the case of the new Quapaw 16-inch line, which is the 16-inch line extending from Cotton Valley station, a distance of about 15 miles to the eastward. This line, I believe,

was laid in 1931. The actual cost to the company was $52,899. Our figure comparable with this was $43,147. Adding the couplings our figure is $51,841. Mr. Black's figure is $53,842.

"Q. And in the St. Joseph 16-inch line, which is a 16-inch line extending from a point near Lawrence, Kansas, in a northeasterly direction towards St. Joseph, the actual cost to the company was $62,244?

"A. Yes, sir; our comparable figure is $48,746, adding the joints, our figure becomes $53,582, and Mr. Black's figure is $43,803. In the case of the southern trunk, 16-inch line, this is a 16-inch line extending eastward from Grabham station, a distance of 12 or 15 miles. The actual cost to the company was $95,548, our cost, or the cost used in our valuation $95,622, adding the joints, our figure becomes $111,172. Mr. Black's figure is $86,459. That line was also laid, I believe, in 1931.

"Chairman Greenleaf: You are explaining, are you, the method of adding the couplings? I do not understand that. You say the cost to the company is $95,548?

"A. That is correct. That does not include all items of cost which we have included in our valuation, Mr. Greenleaf.

"Chairman Greenleaf: When you say cost to the company, that don't mean all the cost?

"A. No, sir; that was labor only, and in order to make these figures comparable with Mr. Black's we have had to add in the cost of the couplings, which is material, or in case it happens to be a weld, the cost of the weld.

"Chairman Greenleaf: Now, this first figure of $95,448, at Grabham station, you gave that as the cost to the company?

"A. That is correct.

"Chairman Greenleaf: That includes the pipe and the labor?

"A. No, sir; only the labor, no pipe has been included in those figures, merely labor costs.

"Chairman Greenleaf: And then, the $95,622——

"A. Is the figure which we have used in our valuation, which compares with this actual cost to the company.

"Chairman Greenleaf: Now, then, in the $111,000 plus, [fol. 497] you have added, you say, couplings there?

"A. We have added couplings to make it comparable with Mr. Black's figures, because Mr. Black included his

couplings with the line and if we did not do that, the figure would not be comparable.

"Chairman Greenleaf: It was not clear to me, that was all, I just wanted to get an understanding of it.

"The Witness: In the case of the Topeka 16-inch line, that is a 16-inch line extending from Lawrence, Kansas, to Topeka, the cost to the company for labor was $180,345. The cost as reflected in our valuation for labor was $166,415. If we add to this the cost of the joints, our figure becomes $192,177. Mr. Black's figure is $144,869. The Dillworth-Wellington 20-inch line, the cost to the company was $174,894, our comparable figure to this is $162,915; adding the joints, this figure becomes $176,595. Mr. Black's figure is $163,799. In the case of the Ottawa-Lawrence 20-inch line, that is a 20-inch line extending from Ottawa, Kansas, to Lawrence, Kansas. The cost to the company of the labor was $175,005. Our comparable figure was $151,602. Adding the joints, this figure becomes $177,072, which compares with Mr. Black's figure of $142,030. In the case of the Pampa-Wichita line, this is a line extending from the Pampa Field in Texas, to Wichita, Kansas. The cost to the company was $1,547,013. Our comparable figure to this is $1,832,822. Adding the couplings, or the joints, our figure becomes $2,210,633; Mr. Black's figure is $2,052,519, and in connection with that line I might say it is a well known fact, and has never been disputed, that the contractor lost an amount on that line so that he has never built another major pipe line in this area.

"Q. Is that the extent of your investigations?

"A. That is the list.

"Q. Now, taking this—taking these exhibits, Mr. Eastman, how do the figures you have used in your valuation when worked out, compare with the actual experience of the company on costs? I notice in some you are high and in some you are low. How does it average up over the whole thing?

"A. Based on these lines, I would say that our figures average slightly less than the actual cost to the company; that is, with the exception of this Pampa-Wichita line on which we know the contractor lost a huge some of money.

"Commissioner Hill: What is it, including that?

"A. Including that, I believe they are just about the same.

"Commissioner Hill: Did you total those figures to show what the grand total was?

"A. No, sir; I have not totaled these; that can be done."

There was introduced as exhibit 82, a comparison of costs on construction of the Wichita Ottawa 20 inch line, otherwise known as line "G". Exhibit 82 is a comparison of costs of this line to the company, taken from the company's investment record by C. H. Montgomery, and compared with the allowances by Black in his exhibits 42A, B and C, and with the allowances by Hamilton in his exhibits 17A and B. A comparison with respect to rights of way and damages is as follows:

Cost as per company job order 12,145	$38,427.40
Black's valuation	54,489.00
Hamilton's valuation	191,775.00

The following exhibit 82 introduced by Montgomery shows in the column headed "As per company J. O. [fol. 4981] 12,145", the actual cost of the construction of the Wichita Ottawa 20-inch line; in column headed, "As per Black and Veatch" is shown the cost of construction of the Wichita Ottawa 20 inch line as found by Black and Veatch, and the column headed "As per F. C. Hamilton Valuation" there is stated Hamilton's estimate of the reconstruction new of said line as follows:

Comparison of Costs on Construction of Wichita-Ottawa 20-inch Line

	As per company	As per Black & Veatch	As per F. C. Hamilton valuation
1. Materials	$2,129,143.27		
Freight	38,202.17		
Warehouse expense	602.20		
	$2,167,947.64	$2,029,812	
2. Labor	806,310.82		
Garage, teaming and trucking	9,797.92		
	$816,108.74	1,008,340	
	$2,984,056.38	$3,038,152	$3,572,723
3. Right of way and damages	58,427.40	54,489	191,775
A	$3,042,483.78	$3,092,591	$3,764,498

	As per company	As per Black & Veatch	As per F. C. Hamilton valuation
4. Engineering	$302,768.30	$154,630	*$178,636
B			$3,943,134
5. Legal	2,150.49	#61,852	:19,715
Expense Accounts	11,783.71		
Incidental expenses	4,378.92		##39,431
Telephone	744.15		
B	$3,304,309.35	$3,309,073	$4,002,280
6. Interest	24,444.01	198,544	320,182
Totals	$3,388,753.36	$3,507,617	$4,320,460
Deduct items not charged to main line construction	13,643.26		
	$3,375,110.10	$3,507,617	$4,320,460

* 5 per cent of line B column "Hamilton" x $3,572,723.
# Calculated at 2 per cent of A column "Black & Veatch," and includes administration expense x $3,092,591.
: One-half of 1 per cent of line B column "Hamilton" x $3,943,134.
Applies to $3,943,134 at 1 per cent.

[fol. 499] Eastman compared labor costs to the company with labor costs used by Hamilton in exhibit 17, and by Black in exhibit 41, on eleven major pipe lines, as shown by the following tabulation:

Line	Company labor	Hamilton		Black,
		Labor	Labor and couplings	Labor and couplings
Hutchinson-Superior	$355,893	$382,744	$429,343	$348,436
Fort Scott 8"	202,184	180,961	194,736	139,639
Springfield 10"	380,394	442,570	489,809	343,085
St. Joseph 12"	144,683	164,624	190,224	157,268
Quapaw 16" (new)	52,809	43,147	51,841	53,842
St. Joseph 16" (new)	62,244	48,746	53,582	43,803
Southern Trunk 16" (new)	95,548	95,622	111,172	86,459
Topeka 16"	180,345	166,415	192,177	144,869
Dilworth-Wellington	174,894	162,915	176,595	163,799
Ottawa-Law. Jct. 20"	175,005	151,602	177,072	142,050
Pampa-Wichita 20"	1,547,013	1,832,822	2,210,633	2,052,519
Totals	$3,371,012	$3,672,165	$4,277,184	$3,675,769

[fol. 500] To make the company's total for the eleven lines comparable with Black's total, Black arrived at the cost of couplings and welds in those lines by deducting Hamilton's allowance for labor of $3,672,165, from his allowance for labor, couplings and welds of $4,277,184, giving $605,019 for couplings and welds; adding this to the company total for labor of $3,371,012, he arrived at $3,976,031 as the company labor total, including couplings, and welds, and arrived at comparable totals as follows:

Company labor cost plus—

Hamilton's couplings and welds	$3,976,031
Hamilton—labor cost, including couplings and welds	4,277,184
Black, labor cost, including couplings and welds	3,675,769

Black prepared the following tabulation, which is a comparison of major labor items involved in pipe line construction, not including painting labor in Black's and Hamilton's valuation:

[fol. 501]

Size of pipe, inches	4½	6⅝	8⅝	10¾	12¾	16	18	20
Weight, pounds per foot	10.790	18.974	24.696	28.035	33.375	42.053	70.589	65.708
Excavation, per foot of line:								
Hamilton	.0540	.0670	.0840	.1030	.1200	.1490	.1670	.1840
Black	.0470	.0502	.0535	.0693	.0798	.1010	.1062	.1189
Backfilling, per foot of line:								
Hamilton	.0251	.0348	.0410	.0476	.0547	.0662	.0745	.0833
Black	.0108	.0115	.0122	.0156	.0182	.0231	.0243	.0272
Hauling, stringing, laying, per foot of line:								
Hamilton	.0563	.1026	.1335	.1515	.1804	.2273	.2615	.2552
Black	.1484	.2372	.2470	.2804	.2920	.3154	.5294	.4025
Jointing, per foot of line:								
Hamilton based on 18-inch lengths	.0883	.1189	.1422	.1767	.2072	.2306	.3706	.4272
Black	.1100	.1600	.2000	.3300	.3600	.4700	.5300	.5100
Hamilton's Total	.2257	.3233	.4007	.4788	.5623	.7731	.9936	1.0497
Black's Total	.3162	.4589	.5127	.6955	.7500	.9095	1.1799	1.0596

[fol. 562] A comparison of the valuation as of Black and Hamilton for this account shows there is a difference of 4½ per cent in the allowances between Black and Hamilton for omissions and contingencies on $26,391,305 worth of pipe, in accounts 1314 and 1333. On the remainder of the difference in these two accounts, or $24,409,515, Hamilton allows a minimum difference for omissions and contingencies of 3 per cent more than Black. Black's allowances for omissions and contingencies on pipe in ½ of 1 per cent on $26,931,305, or $134,657. Hamilton's allowance for omissions and contingencies on this same item was $1,446,565. Black's allowances on the remainder of this account was a maximum of 2 per cent on $24,409,515, or $488,190, and Hamilton's allowance for the remainder of this account was 5 per cent, or $1,220,475. Black's total allowance for omissions and contingencies was $622,847, as against a total allowance by Hamilton of $2,667,040.

Black, engineer for the Commission, prepared the following table comparing overheads on pipe in Accounts 1314 and 1333, showing the overheads used by Hamilton in his valuation and the overheads shown by Mr. Black in his valuation:

[fol. 503]

Comparison of Overheads on Pipe in Accounts 1314 and 1333

	Hamilton			
	Field lines	Main lines	Black, field and main lines	
1. Base Value	1.000000	1.000000		1.000000
2. Warehousing—5% of field-line pipe only	0.050000		½ per cent of item 1	0.005000
3. Purchasing, pipe only			1 per cent of item 1	0.010000
4. Supervision and inspection			1½ per cent of item 1	0.015000
5. Subtotal, items 1 to 4, inclusive	1.050000	1.000000		1.030000
6. Omissions and contingencies—5 per cent of item 5	.052500	.050000	½ per cent of item 1	.005000
7. Subtotal, items 5 and 6	1.102500	1.050000		1.035000
8. Engineering—5 per cent of item 7	.055125	.052500	5 per cent of item 7	.051750
9. Subtotal, items 7 and 8	1.157625	1.102500		1.086750
10. Organization—½ per cent of item 9	.005788	.005513	¼ per cent of item 7	.007763
11. Law expense—½ per cent of item 9	.005788	.005513	2 per cent of item 7	.020700
12. Taxes—1 per cent of item 9	.011576	.011025	1.36 per cent of item 7	.014076
13. Miscellaneous construction expense—1 per cent of item 9	.011576	.011025		
14. Subtotal, items 9 to 13, inclusive	1.192353	1.135576		1.129289
15. Interest—8 per cent of item 14	.095388	.090846	12 per cent of item 10, 6 per cent of items 14 less 10	.068223
16. Subtotal, items 14 and 15	1.287741	1.226422		1.197512
17. Cost of financing—4 per cent of item 16	.051510	.049057		
18. Subtotal, items 16 and 17	1.339251	1.275479		1.197512

[fol. 504] As a check upon the estimates of the respective engineers on rock excavation in Line "G", being a 20-inch line between Wichita and Ottawa, after the decision by the Commission, the plaintiffs accompanied by Geo. P. Reintjes and engineers of the Commission, made actual borings and tests of rock along line "G" in order to determine the actual per cent of pick rock, shoot rock and earth which would be encountered in actual construction. In reference to this new field survey, Mr. Reintjes made an affidavit, stipulated to be considered as his testimony, setting forth his contentions as follows:

"We submit herewith a report of the amount of the rock and earth excavation encountered during the construction of pipe line G between Ottawa and Wichita, Kansas, as estimated on the basis of a recent survey of the entire line. This survey involved actual tests of the nature of the soil along the entire line. The survey was conducted by a party consisting of one of your engineers, Mr. Robert L. Kiddoo; Mr. J. F. Brown, an engineer in the organization of Black and Veatch; the writer; two members of our organization; with assistants for drilling furnished by the pipe line superintendents of the various divisions of the line.

"The rock encountered between Ottawa and Emporia was similar in formation to the Kansas City formation known as the crusher ledge, and a flinty limestone ledge known as the bull ledge, with occasional sandstone outcroppings.

"West of Emporia, the rock in general consisted of an upper formation from 6" to 3'0" thick of very dense flint rock. Underlying it was a dense limestone containing considerable flint or quartz. Below this were several ledges of limestone from 4" to 6" in thickness each. Beneath this was what is known as the Cottonwood Falls limestone which ranged in thickness from 20" to 6'0". The Cottonwood Falls limestone, as well as the ledges immediately above, were comparatively level. The flinty limestone ledge, in places, followed the contour of the hills. The same is true of the flint rock.

[fol. 505] "We dug or drilled two hundred and ninety one holes along the pipe line with a view of using such findings, together with an observation of the amount of rock exposed,

in the pipe line backfill; and exposed ledge outcroppings in determining an estimate of the average amount of rock in each section or square mile traversed by the line. Where the nature of the soil was such that an average estimate could not be placed upon a mile of line smaller lengths ranging down to an eighth of a mile were used. Where rock ledges of some extent were encountered, in order to explore the depth of the ledge, holes were drilled into the rock to a depth below the required trench depth, at intervals of approximately a mile.

"In our estimates we did not consider this strata of shell rock which in our estimation could be broken and removed by the machine ditcher. Nor was the consideration given to extra depth necessitated by highway crossings, etc.

"It is our experience that rock cannot be excavated to a neat depth. It is necessary to excavate by blasting to a depth somewhat below the specified trench depth and backfill to grade with a cushion of earth. Our findings of the quantities of rock summarized by counties as a percent of the specified dimensions of the trench do not consider this extra depth, or overcut. However, in an additional column captioned "Overcut", the amount of such extra excavation expressed as a percent of the specified trench dimensions is tabulated. In the last column are tabulated the percentages of classified excavation allowed by Black.

"We feel that our estimates of the amount of pick and sheet rock in this line are conservative, and that the actual amount of rock taken out by the Contractor in the execution of his contract was probably in excess of these figures.

[fol. 506]

Summary of Rock Excavation, Line G, Wichita–Ottawa 20"

County	Length		Shoot rock		Pick rock		Total			
	Main line	Containing rock	Equivalent Length	%	Equivalent Length	%	Equivalent Length	%	Overcut %	Black's allowance %
Butler	211,144	154,313	49,353	23.37	130	.06	49,483	23.44	10.06	10.01
Chase	83,388	73,172	42,399	50.85	270	.32	42,669	51.17	11.96	14.95
Coffey	36,369	2,380	216	.59	...	...	216	.59	.89	2.00
Franklin	87,566	39,719	17,013	19.43	...	...	17,013	19.43	6.18	12.48
Lyon	104,635	27,928	9,772	9.34	...	...	9,772	9.64	3.64	[illegible]5
Osage	97,964	36,225	15,511	15.83	66	.07	15,579	15.90	5.01	6.24
Sedgwick	22,592	1,200	82	.36	...	...	82	.36	.79	1.24
Totals	643,658	334,937	134,346	20.87	466	.07	134,814	20.94	7.09	10.46

[fol. 507]

Survey of Rock Excavation, Wichita-Ottawa 20", Line 6

County	Length Main line	Shoot rock		Pick rock		Total		Black %
		Equivalent length	%	Equivalent length	%	Equivalent length	%	
Butler	211,144	49,353	23.37	130	.06	49,483	23.44	10.01
Chase	83,388	42,399	50.85	270	.32	42,669	51.17	14.95
Coffey	36,369	216	.59	...	...	216	.59	2.00
Franklin	87,566	17,013	19.43	...	...	17,013	19.43	12.48
Lyon	104,635	9,772	9.34	...	...	9,772	9.34	14.95
Osage	97,964	15,511	15.83	68	.07	15,579	15.90	6.24
Sedgwick	22,592	82	.36	...	...	82	.36	1.24
Total	643,658	134,346	20.87	468	.07	134,814	20.94	10.46

[fol. 508] There followed in Reintjes' affidavit details showing the exact location of the 291 holes drilled and the exact conditions encountered, which we deem unnecessary to set out herein.

In reference to this new field survey, Black made an affidavit stipulated to be considered as his testimony setting forth his contentions as follows:

"That I am familiar with Hamilton's exhibits 17a and 17b showing the linear feet of shoot rock and pick rock in the excavation for pipe lines in the transmission systems of the Cities Service Gas Company, the Cities Service Gas Pipe Line Company, and the American Pipe Line Company.

"That when the linear feet of shoot rock and pick rock on each size of pipe line in Hamilton's exhibits 17a and 17b is multiplied by the cubic yards of excavation per linear foot of ditch corresponding to the widths and depths of ditches used by Hamilton in the calculation of costs per linear foot of pipe line in shoot rock at $7.38 per cubic yard, and of pick rock at $4.01 per cubic yard, the results show totals for the system, including line G, of 256,861 cubic yards of shoot rock, and 577,428 cubic yards of pick rock; that the total cubic yards, and total cost of shoot rock and pick rock as calculated from Hamilton's exhibits 17a and 17b, and total cubic yards and total cost of classified excavation covering all classes of rock excavation as calculated from Black's exhibits 41a, 41b, and 41c, is as shown by the following tabulation:

[fol. 509]

Item	Hamilton		Black	
	Cubic yards	Total cost	Cubic yards	Total cost
Shoot rock	256,861	$1,895,634	.....	.....
Pick rock	577,428	2,315,486	.....	.....
Rock, all classification	.....	.....	508,046	$1,270,115
Totals	834,289	$4,211,120	508,046	$1,270,115
Excess—Hamilton over Black	326,243	$2,941,005	.....	.....

"That included in the above tabulation is rock excavation on Line "G", between Wichita and Ottawa, as set out in the following tabulation:

Item	Hamilton		Black	
	Cubic yards	Total cost	Cubic yards	Total cost
Shoot Rock	35,760	$263,990	.....	.....
Pick rock	36,722	147,584	.....	.....
Rock, all classifications	.....	.....	24,000	$60,000
Totals	72,482	$411,574	24,000	$60,000
Excess—Hamilton over Black	48,482	$351,574	.....	.....

[fol. 510] "That Hamilton in calculating the unit costs of pick rock and shoot rock in his exhibits 17a and 17b applied $7.38 per cubic yard for shoot rock and $4.01 per cubic yard for pick rock, to the cubic yards per linear foot of trench determined by the dimensions of trenches set out in exhibit 73, except that in pick rock he used a trench depth 4 inches greater than shown by the exhibit, and that wherever shoot rock or pick rock was found it was calculated as being solid from top to bottom of the trench.

"That I used trench widths and depths shown on pages 18 to 23, inclusive, of my exhibit 42, and that in determining these dimensions I had available 43 pipe-line construction contracts of the Cities Service Gas Company and the Cities Service Gas Pipe Line Company covering a total of 1,673 miles of pipe lines constructed in Texas, Oklahoma, Kansas, Missouri, and Nebraska, towit:

"Contract No. 7736, filed as exhibit 38, covers 242.13 miles of the 20-inch line and 26.46 miles of 12-inch *pipe in* river crossings between Pampa and Wichita, in Sedgwick, Sumner, Harper and Barbar counties, Kansas; Alfalfa, Woods, Woodward, and Ellis counties, Oklahoma; Hamphill, Roberts, and Gray counties, Texas.

"Contract No. 7895, filed as exhibit 81, covers 25.11 miles of 20-inch pipe line, 4 miles of 16-inch, 0.8 miles of 4-inch, 1.73 miles of 6-inch, and 4.48 miles of 8-inch pipe lines, in Gray, and Carson counties, Texas.

"Contract No. 8072, filed as exhibit 80, covers 139.62 miles of the Wichita-Ottawa 20-inch pipe line, made up of 121.9 miles of 20-inch and 14.52 miles of 16-inch and 3.20 miles of 12-inch pipe line in river crossings, in Butler, Chase, Coffey, Franklin, Lyon, Osage, and Sedgwick counties, Kansas.

"Contract No. 8302, filed in this case as exhibit 78, covers 43.5 miles of 8-inch gas pipe-line in Allen and Bourbon counties, Kansas, between the Petrolia station and Fort Scott.

"Contract No. 8314, filed in this case as exhibit 79, covers 70.6 miles of 10-inch, 8.7 miles of 3-inch, 0.39 miles of 2-inch, and 3.3 miles of 6-inch main and branch lines in Newton, Lawrence, Christian and Greene counties, Missouri.

"Contract No. 6553, covering 33.71 miles of the Davenport-Lindley line in Creek and Lincoln counties, Oklahoma,

and consisting of 4.05 miles of 8-inch, 8.70 miles of 10-inch and 20-96 miles of 16-inch pipe line.

"Contract No. 7419, covering 5.83 miles of 6-inch pipe line in Okfuskee county, Oklahoma.

[fol. 511] "Contract No. 7434, covering 12.66 miles of 6-inch and 12.02 miles of 8-inch pipe in the Bearden-Papoose-Seminole gas-gathering system in Okfuskee, Hughes and Seminole counties, Oklahoma.

"Contract No. 7511, covering 30.14 miles of 16-inch gas line in Creek, Okfuskee, and Seminole counties, Oklahoma.

"Contract No. 7524, covering 6 miles of 12-inch line in Seminole, Okfuskee and Hughes counties, Oklahoma.

"Contract No. 7563, covering 10.18 miles of 8-inch gas pipe line in Kay and Grant counties, Oklahoma.

"Contract No. 7612, covering 5 miles of 12-inch line in Seminole county, Oklahoma.

"Contract No. 7799, covering 14.63 miles of 12-inch gas pipe line in Osage county, Oklahoma.

"Contract No. 7846, covering 11.96 miles of 16-inch line in Allen county, Kansas.

"Contract No. 7927, covering 2.62 miles of 6-inch line in Hughes county, Oklahoma.

"Contract No. 8028, covering 5.33 miles of 8-inch gas line in Gray county, Texas.

"Contract No. 8059, covering 2.06 miles of 8-inch and 6-inch line in Carson county, Texas.

"Contract No. 8090, covering 5.97 miles of 12-inch line in Leavenworth county, Kansas.

"Contract No. 8091, covering 38.75 miles of 16-inch line in Franklin, Douglas and Johnson counties, Kansas.

"Contract No. 8095, covering 6.67 miles of 8-inch line in Osage county, Oklahoma.

"Contract No. 8123, covering 7.30 miles of 8-inch gas pipe line in Lyon county, Kansas.

"Contract No. 8129, covering 26.93 miles of 12-inch gas line in Leavenworth county, Kansas, and Platte and Buchanan counties, Missouri.

"Contract No. 8149, covering 11.64 miles of 4-inch pipe line between the Wichita-Ottawa 20-inch main line and the Madison, Kansas, gasoline plant, in Lyon and Greenwood counties, Kansas.

"Contract No. 8210, covering 15 miles of 4-inch and 10-inch line in Newton county, Missouri.

"Contract No. 8247, covering 8.31 miles of 16-inch and 1.23 miles of 2-inch line in Washington and Nowata counties, Oklahoma.

"Contract No. 8282, covering 19.47 miles of 20-inch line and 15.07 miles of 16-inch in line Douglas and Franklin counties, Kansas.

"Contract No. 8283, covering 9.23 miles of 6-inch line in Seminole county, Oklahoma.

"Contract No. 8289, covering 28.42 miles of 8-inch line in Rice and Reno counties, Kansas.

[fol. 512] "Contract No. 8292, covering 28.42 miles of 8-inch line in Kay, Noble and Logan counties, Oklahoma.

"Contract No. 8321, covering 15.81 miles of 12-inch, 4.04 miles of 10-inch and 1.29 miles of 6-inch line in Logan county, Oklahoma.

"Contract No. 8328 and 8328-A, covering 39.5 miles of 8-inch, 11.4 miles of 6-inch, 16.62 miles of 4-inch and 8.86 miles of 2-inch line of the Atchinson Falls City, Neb., line, in Atchinson and Brown counties, Kansas, and Richardson, Nebraska.

"Contract No. 8341, covering 10.86 miles of 6-inch line in Okfuskee county, Oklahoma.

"Contract No. 8376, covering 39.19 miles of 20-inch and 10 miles of 24-inch line from Logan county to Oklahoma City, Oklahoma.

"Contract No. 8399, covering 5.90 miles of 16-inch line in Douglas and Shawnee Counties, Kansas.

"Contract No. 8400, covering 40.29 miles of 2-inch, 14.55 miles of 3-inch, 58.94 miles of 4-inch and 116.28 miles of 8-inch line in Rice, Ellsworth, Lincoln, Mitchell, Osborn, Jewell and Smith counties, Kansas, and Nuckolls county, Neb.

"Contract No. 9421, covering 14.96 miles of 16-inch line in Montgomery and Labette counties, Kansas.

"Contract No. 8460, covering 5 miles of 6-inch line in Carson and Gray counties, Texas.

"Contract No. 8466, covering 31.37 miles of 20-inch line between Dilworth, Okla., and Wellington, Kans., in Kay county, Oklahoma, and Sumner county, Kansas.

"Contract No. 8467, covering 109.23 miles of 12-inch line between Ottawa, Kansas, and Sadalia, Mo., in Franklin and Miami counties, Kansas, and Cass, Johnson and Pettis counties, Missouri.

"Contract No. 8476, covering 9.09 miles of 16-inch line in Douglas and Leavenworth counties, Kansas.

"Contract No. 8481, covering 25.73 miles of 3-inch line in Lincoln and Ottawa counties, Kansas.

"Contract No. 8501, covering 44.17 miles of 8-inch, 21.90 miles of 6-inch, 16.90 miles of 4-inch and 7.65 miles of 3-inch line in Johnson, Carroll, Lafayette, and Saline counties, Missouri.

"That I made my classification of excavation by inspection of the location of the lines and by my knowledge of the territory through which these lines ran; that in addition to allowing earth excavation on all lines to the full depth of trench at 35 cents per cubic yard, I also allowed in the same ditch classified excavation to cover all classes of rock, including shoot rock or pick rock, at $2.50 per cubic yard for whatever per cent of the excavation I found as rock, or, in other words, I allowed $2.85 per cubic yard for rock excavation.

"That T. R. Jones, who constructed line G between Wichita and Ottawa, under a contract filed as exhibit 80, testified that "a little over 75 cents' per linear foot was [fol. 513] a fair price for rock excavation on this line in a trench 28 by 40 inches (tr. 2247); that this is equivalent to a price of $2.60 per cubic yard for solid rock. (Agreed statement of facts and agreed abstract of the evidenec. P. 35.)

"That from October 7 to 16, inclusive, 1932, a field party under the direction of George P. Reintjes and Robert L. Kiddoo for the respondent, with J. P. Brown as an observer for my office, made measurements at 291 points along line G between Wichita and Ottawa for the purpose of determining the actual quantities of rock involved in its construction; that the points at which these measurements were made were selected primarily because rock showed in the trench backfill, and that all other sections of the line were excluded from the survey on the theory that only earth excavation would be encountered; that 234 soundings were made to determine the depth of cover over the pipe, and 291 soundings were made to determine the depth to rock in undisturbed earth, and that the thickness of rock was generally determined by deducting the depth to rock in undisturbed earth from the depth of pipe cover plus the 20-inch outside diameter of the pipe; that 38 borings

were made through the rock to the plane of the pipe bottom.

"That although this survey established the fact that the depth of trench in line G averaged 48.72 inches instead of 44 inches, the depth used by both Hamilton and Black in the calculation of rock quantities in Hamilton's exhibits 17a and 17b and in Black's exhibit 41a and 41b, that Reintjes calculated the per cent of rock exclusive of alleged overbreak on the basis of a 44-inch depth of ditch instead of on the actual and greater depth of ditch determined by the resurvey; that, for illustration, Reintjes shows that at survey hole No. 149, Butler county, Kansas, the depth of earth over rock was 34 inches, and that the thickness of rock above pipe bottom was 18 inches, the depth of ditch to pipe bottom was 52 inches; that Reintjes calculates the percentage of rock at this point by dividing the 18 inches by 44 inches which results in 40.9 per cent of rock instead of 34.6 per cent, the correct figure as shown by this test hole if the 18 inches, the depth of rock, is di-
[fol. 514] vided by 52 inches, the actual depth of trench.

"That Reintjes estimates it is necesary to excavate the trench in rock 6 inches below pipe bottom to allow for alleged overbreak, and that he calculated this per cent of overbreak on the basis of a 44-inch depth of ditch, instead of on the actual and greater depth determined by the survey, and that using survey hole No. 149, Butler county, Kansas, this percentage as calculated by Reintjes is 6 inches divided by 44 inches, or 13.6 per cent, instead of 10.3 per cent, which figure results from the division of 6 inches by 58 inches, the actual depth of trench including alleged overbreak; that the 7.09 per cent of alleged overbreak in the tenth column of Reintjes' survey summary is obtained by applying the percentage found by dividing 6 inches of overbreak on 334,937 feet of line G covered by the survey by a trench depth of 44 inches and applying it to the total length of 643,658 feet in line "G".

"That the resurvey of line G disclosed no basis for the calculation of overbreak, if any, below the bottom of the pipe as laid. That the contractor on Line G was required to cover this line a specified minimum cover in "shoot rock" and a specified minimum cover in earth and "pick rock," and that he was required to perform all the ditching and backfilling in all classes of excavation, as well as certain other construction operations, for a specified price per foot of line regardless of the character of quantities

of materials excavated in order to secure the minimum cover specified. (Exhibits 80 and 77.) That the resurvey of line G shows the following quantities of classified excavation and the quantity of rock excavation included in Hamilton's exhibits 17a and 17b and in Black's exhibits 41a, 41b and 41c.

[fol. 515]

Item (Vol. 1)	Hamilton Exhibits 17a and 17b (Vol. 2)	Black Exhibits 41a, 41b and 41c (Vol. 3)	Resurvey Reintjes excluding overbreak (Vol. 4)	Resurvey Reintjes including overbreak (Vol. 5)	Resurvey Brown (Vol. 6)
Trench width and depth in earth and "pick rock"	39" x 44"	30" x 44"	39" x 44"		39" x 50"
Trench width and depth in "shoot rock"	39" x 40"	30" x 44"	39" x 44"		39" x 48.7"
Cubic yards of "shoot rock"	35,771		48,655	65,901	46,619
Cubic yards of "pick rock"	30,804		163		170
Cubic yards of rock of all classifications	79,575	94,000	48,818	65,901	46,789

[fol. 516] "That if the allowance for rock on line G is made on the basis of Brown's calculations from the resurvey there should be added to Black's total allowance for account 1333 —

46,789 cu. yds. of rock @ $2.50, or	$116,972.50
Less 24,000 cu. yds. of rock @ $2.50	60,000.00
Or a net addition of	56,972.50

"That if alleged overbreak should be added on the basis of Reintjes' calculations there should also be added 16,546 cu. yds. of rock excavation at $2.50 or a total of $41,365.

"That I have made a calculation of the average outside diameter of pipe in the transmission systems involved herein and that the average pipe in rock excavation is under 12 inches outside diameter, and if laid in the same location as line G there would be an average, but not an actual, decrease of 8 inches in the depth of rock excavation and an actual decrease of 8 inches in the width of trench, and that the per cents of rock excavation developed by the resurvey of line G cannot fairly be applied to that part of the total system on which rock is encountered.

"That the following tabulation is a summary by counties, showing total trench excavation, total rock excavation, the ratio in per cent of solid rock and "pick rock" to total excavation, as calculated from the date obtained by Brown in the resurvey of Line G. The calculation of the above data by land section is attached hereto.

[fol. 517]

Summary of Counties of Rock Quantities in Line G Calculated from Resurvey of October 7 to 16, 1932.

County	Length along center line			Total trench excavation			Total rock excavation		Ratio of rock excavation to total trench excavation	
	Gross feet	River crossings, feet	Net feet	Total cu. yds.	River crossings, cu. yds.	Net cu. yds.	Solid cu. yds.	Pick cu. yds.	Solid Per cent	Pick Per cent
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
Franklin	91,449	4,332	87,117	39,266.6	1,783.1	37,483.5	4,980.3	0.0	12.97	0.00
Osage	98,635	671	97,964	40,152.6	276.2	39,875.4	5,377.0	24.7	13.48	0.06
Coffey	36,369	0	36,369	14,969.4	0.0	14,969.4	0.0	0.0	0.00	0.00
Lyon	130,195	25,560	104,635	53,153.7	10,520.5	42,633.2	3,088.0	0.0	7.24	0.00
Chase	83,388	0	83,388	32,403.6	0.0	32,403.6	15,169.9	97.5	46.45	0.30
Butler	223,540	12,396	211,144	88,473.3	5,102.2	83,371.3	18,204.5	47.3	22.54	0.06
Sedgwick	22,592	0	22,592	9,298.5	0.0	9,298.5	29.6	0.0	0.32	0.00
Totals	686,168	42,599	643,209	277,717.2	17,682.0	260,035.2	46,629.3	169.5	17.93	0.07

[fol. 518] Interest During Construction

The evidence on Interest During Construction was submitted to the District Court on the following agreed-statement:

"Hamilton allowed for this item $6,337,986.00, which he did not depreciate. Black allowed $4,345,125.00 new and $3,868,428.00 depreciated. The Commission allowed for the item $3,883,282.00 the difference between that allowance and the amount claimed by Hamilton being $2,454,704.00.

"The allowance made by the Commission is the allowance made by Black adjusted in accordance with changes made in his valuation of the property.

"As to the basis for his allowance Black testified as follows:

* * * 'Q. The next item is interest during construction $4,345,125.00. How did you arrive at that?

'A. Interest during construction has been arrived at on the basis of a two-year construction period, using an interest rate of six per cent. I have assumed, however, that all land and rights of way would necessarily be acquired early in the construction period; for that reason I have allowed two years' interest, or twelve per cent on all lands and all rights of way.

'Q. Is that depreciated?

'A. Interest during construction is applied also to all property accounts plus engineering and superintendence, administrative and legal expenses and taxes during construction.

'Q. In other words to all items appearing on this summary above the item of interest during construction?

'A. Excepting preliminary organization expenses, that is not applied there.

'Mr. Stone: On the rest of the construction an average of two years in the one year?

'A. Yes, sir. * * *

'Q. Is that depreciated?

'A. Yes, sir.'

"Black further testified that he allowed interest at the rate of 6% for one year on all physical property except land and rights-of-way on which he allowed 6% for two years or a total of 12%; that he took two years as the con-

struction period; that he assumed part of the system would be placed in operation before the completion of the entire project and for that reason eliminated half the construction period; that he did this on the theory that 'you have your investment only for half the period; * * * that you are only going to have your investment in certain items that enter into the property of this kind during half of the construction period and for that reason 6% is the interest return on the entire construction period, just based on the average time'; that in his opinion the rate of interest [fol. 519] during construction should be different from the rate of return on the project after it is placed in operation. The witness was not asked and did not state any reason for this difference in rate of return other than his own opinion.

"Hamilton testified that he used 8% based on a two-year construction period and therefore allowed 8% for one year; that his 8% was figured on the same amount as that on which organization and legal expenditures are figured plus total of organization, legal expenditures, taxes during construction and miscellaneous construction expenditures; that he did not assume the plant would be in operation during the construction period of two years and that no income would result from operation during that period."

Going Value

It was agreed by the parties before the District Court that the following agreed statement on going value should be submitted as the evidence on that account:

"Black allowed in his valuation for this item $3,820,000.00 and Hamilton $8,898,532.00, the difference between the two engineers being $5,078,532.00. The Commission found a going value of $2,000,000.00 on the reasoning set out in the opinion at pages 85 to 88.

"In regard to going value, Black testified (T. pages 1873-1874) as follows:

'* * * Q. The last is going concern value, $3,820,000.00. How did you arrive at that amount?

'A I have considered going concern value at it is normally considered, I think, as being the difference between a plant all ready to operate and not operating, and a plant all ready to operate with customers attached. I have taken as

the best measure of certain items of that going value the company's operating experience, and briefly I have allowed in arriving at this figure used here, $15,000.00 for the books and records of the company, I have allowed $1,020,000.00 for organization of the operating company, that is the organization of the company, and I have allowed interest and depreciation on idle plant, plant that would be idle during the period this company is acquiring its business, that is between the end of the construction period and the time all business is attached, in the amount of $2,784,645.00, added to the two other amounts of $15,000.00 and $1,020,000, gives $3,819,645.00, which I have applied as $3,820,000.00.

[fol. 520] 'Q. Is that depreciated?

'A. No sir, it is apportioned among the properties of the various states directly in proportion to the cost of reproduction of property in those states bears to the cost of the reproduction of the total property. * * *"

"And again on pages 2178 and 2181 as follows:

"* * * I have computed my allowance for going concern value on the basis that it is best measured by the cost of reproducing the business of the company and I have allowed in my calculations for going concern value for books and records of the company, for organization, for interest on idle plant and for depreciation on idle plant.

'Q. Those are the items that have entered into the total you have given in your calculation?

'A. Yes, sir, $3,820,000, rounded out.

'Q. Have you those figures broken down into the different items entering into the totals?

'A. Yes, sir.

'Q. Let us have those, please?

'A. I have books and records of the company at $15,000.00. These books of course are the records or whatever they may be, are in addition to the property records, etc., which you have accumulated during the time of your construction. I have allowed $1,020,000 for organization, I have allowed a total for interest on idle plant and depreciation on idle plant of $2,784,645.

'Q. That is 6% interest?

'A. No, that is on the basis of 8%.

'Q. And what rate of depreciation, please?

'A. Two and one-half per cent.

'Q. What was that amount?

'A. Two and one-half.

'Q. I mean, the amount of this two items in dollars?

'A. $2,784,645.

'Q. What are the other items, please? Is that all of that, does that make the total amount allowed?

'A. This is—yes, it totals to $3,819,645, and we have used $3,820,000.

'Q. The 8 per cent you have allowed for interest and 2½ per cent for depreciation, would make a total of 10½ per cent that you have applied to the idle plant, is that the idea?

'A. That is true, sir.

'Q. Well, if those two figures total 10½ per cent which are applied to the idle plant it would have to be $26,500,000 to give that figure by applying 10½ per cent, would it not?

'A. I did not apply it that way.

'Q. I would like to have that?

'A. Well on the basis of having 50 per cent of the business attached at the end of the construction period and 100 per cent at the end of the second year, I have in my calculation for interest on idle plant, I have 30 per cent of my plant idle for one year and 5 per cent idle for one year, at 8 per cent, that works out to .028, as applied to the entire property, and results in the figure. I have not separated that figure after applying it to the total property, but I have added all my depreciation on idle plant in the same calculation, that is in percentage.

[fol. 521] 'Chairman Greenleaf: Just as a matter of information, what is the idle plant? Just what do you refer to there, just roughly?

'A. I am assuming that, in the construction of this property as it exists today, that we are attaching business, certain capacity of this plant that is not required.

'Chairman Greenleaf: I understand now. I did not know to what you referred.

'A. Yes.

'Q. Are you assuming that on the completion of the plant, the entire project, at the end of a two-year period that all of its business will be attached at that time?

'A. No, sir, 50 per cent of it.

'Q. Fifty per cent?

'A. Yes, sir.

'Q. Then at the——

'A. You are talking about the construction period now?

'Q. Yes, you assume two years' construction period?

'A. Yes, sir.

'Q. At the end of two years, the project will be completed?

'A. That is correct.

'Q. What percentage of business do you assume will be attached at that time?

'A. Fifty per cent at that time.

'Q. And at that time 50 per cent of the plant would be idle?

'A. Yes, if there is 50 per cent of it not built—you mean at the end of the construction period?

'Q. Yes, 50 per cent of the plant would still be idle and earning nothing on the investment?

'A. Yes, that is right. * * *'

"Hamilton testified, on cross-examination as follows:

'* * * Q. Now, we come to going concern value. That is $8,898,532.00?

'A. Yes, sir.

'Q. Is that a percentage of anything?

'A. That is 10 per cent.

'Q. Of what figure?

'A. That is 10 per cent on all of the items up to and including the cost of financing, but excluding working capital and materials and supplies.

'Q. Working capital and materials and supplies is the only thing excluded?

'A. That is the only thing excluded, yes, sir.

'Q. How did you arrive at that amount?

'A. I have just taken 10 per cent of the physical property value for this particular case, for that item.

'Q. You have not itemized it?

'A. No, sir, I have not itemized it in any way.

'Q. You have not taken into consideration the fact that in the reproducing new this system, that you are wholesaling gas and that you have your markets already provided?

'A. You could not possibly have your markets already [fol. 522] provided, because it takes a distributing company at least three years to get their customers up to a

reasonable consumption of gas, after they have started putting in the appliances. You have a place to sell gas, but you cannot sell it until they in turn get their customers to buying it.

'Q. You would not include in this any expenses the distributing companies have?

'A. No, we would include in this no cost the distributing company has to take, because of their expenses in getting customers, but we do include in this cost the carrying pipe line capacity that is idle a portion of the time until you get up to the load for which it was ultimately, or for which it was designed.

'Q. But in this case, here, these distributing companies are already functioning and furnishing gas?

'A. They would not.

'Q. And all that the pipe line company would have to do would be to get the gas to the city gates and turn on the gas, isn't that all they would have to do?

'A. No, for the simple reason that the gas companies would not be functioning and furnishing gas until such time as the pipe line company had——

'Q. You mean their relationship is such that they could not exist without the pipe line companies?

'A. Not as natural gas companies, that is perfectly true.

'Q. Some of these concerns were furnishing gas at the time you purchased them, were they not?

'A. Furnishing——

'Q. Some of these distributing companies?

'A. Of course, because the pipe line had been constructed for years.

'Q. Your company wholesales gas, as I understand?

'A. That is true.

'Q. You don't furnish any gas to domestic consumers?

'A. There is some slight exception to that where we run through farms, or something like that but they don't mean anything.

'Q. How many customers do you have to which you wholesale gas, in round numbers, I don't care to have it exact.

'Mr. Stone: You mean including distributing companies.

'Mr. Welch: Yes, sir.

'A. I cannot tell, because I don't know how many main line industrial consumers there are. We have some.

'Q. Omitting the main line industrial consumers, how many customers do you have to which you furnish gas.

'A. Oh, I presume at least a hundred.

'Q. For instance, take the City of Wichita, this system does pipe the gas there and turn it over to the distributing company?

'A. To the town border, and in my estimate of a hundred I have included Wichita as one.

'Q. Now what do you include in the elements of going value, Mr. Hamilton?

'A. What I have included in the value of the business attached and operating, and yielding a revenue, and I have done it on the basis of experience with the cost of getting a system into that sort of shape.

[fol. 523] 'Q. As I understand, then, you did not arrive at it by finding the cost of attaching this business.

A. It is partially the cost of attaching the business, and the time of the engineers and others in negotiating the contracts, but that, for a wholesale situation, is a small item. The largest cost is the excess capacity that you will have to have for a period of three years, while your distributing companies are getting up to a point where they use the amount of gas that the size of the system is predicated on.

Q. Do you think that if you should reproduce your plant new and then go to the Wichita distributing company that you would have any trouble negotiating a contract with them to turn them over the gas?

A. No.

Q. Would that be true with reference to the Western Distributing Company?

A. It would be perfectly true, but we would not have any trouble about it, but we would have to determine what amount they had and reach an agreement on that.

Q. Well your plant is constructed here, with the idea of selling all the gas you can get a market for, isn't it?

A. Yes.

Q. So whatever amount they might want you would be very glad to turn it over to them at what you determined to be the price at the gates?

A. That is true, but we would have to arrive at some conclusion as to what that amount would be.

Q. That wouldn't take very long, would it?

A. Yes, it would take some considerable time, and a lot of judgment, if you were going into a town that didn't now have natural gas, you would have to make a pretty careful——

Q. You assume those towns don't have natural gas. We are today talking about the proposition of reproducing this pipe line now.

A. Yes, sir.

Q. You know just exactly where you want to go, you know you want to go to Wichita, you know you want to go to Ottawa, you know you want to go to Topeka, you know you want to go to Kansas City, Missouri, and places of that kind, and so far as that is concerned, there is nothing unknown about that, you know exactly what you want to do, you know that you want to furnish gas at these various towns, because you are building your pipe line up to them, and you know in most of the towns that there is a distributing company there, with a market that wants to buy gas of you, isn't that true?

A. That is very true.

Q. Now in constructing this pipe line, reconstructing this pipe line, if you had to reconstruct it now, what would be the best place to commence after you had your gas fields established, and in view of the fact that you have your gas purchase contracts?

A. It would be at the field. What you would do, as a practical matter, is commence at half a dozen different places as we do. In other words, very seldom will you find a contractor with a force, or equipment ready to take a contract for a whole pipe line. It is let by sections, so you actually commence construction in several different places.

Q. Now having in mind this particular pipe line, where in your opinion would it be best to commence constructing this line and to what points?

A. Well, I think you would commence constructing this at the various fields, and moving toward the towns as rapidly as you could.

[fol. 524] Q. One of the largest fields that you buy gas from is the Oklahoma City Field?

A. Yes, sir.

Q. And that line would be constructed from there among the first, wouldn't it?

A. Yes.

Q. And that line in a short time could be supplying the city of Wichita, I take it?

A. Well, I don't know what you mean by a short time, but you could not get that line constructed in less than a year, I don't believe.

Q. Well, probably when I said short time, that is pretty indefinite, but after you had that line constructed, inside of a year, you could be furnishing gas to the city of Wichita?

A. That would be possible, yes, sir.

Q. Now, while you are building that line, what other lines would you think should be built?

A. I think the Amarillo line would be started, also.

Q. That would also go toward Wichita?

A. Yes, sir.

Q. And what line would you build next?

A. I think we would build north toward Kansas City from the Oklahoma City line, and also across from Wichita toward Ottawa, and into Kansas City.

Q. While you were building those lines from Oklahoma City to Wichita, there is no reason why you could not be engaged in constructing these other lines you have spoken about?

A. That is perfectly true.

Q. They could be all built at the same time?

A. With certain limitation, that is that in such a large project as this, there are only certain contractors with the credit and experience to take the contracts and be able to carry them out.

Q. In other words, on such a vast system there would be some difficulty in getting competent contractors to handle it?

A. Not only contractors, but labor. If you tried to hurry it you would have a lot of contractors bidding for labor and your labor costs would be up.

Q. But in the meantime, while you were constructing this pipe line, it would be good business to commence to furnish the cities along this line just as soon as you could?

A. Just as soon as you could.

Q. Do you know, Mr. Hamilton, how long it took to construct the line from Amarillo to Chicago?

A. From Amarillo to Chicago, it took about fourteen months, as I remember, from the time they started.

Q. That was a 24-inch line, as I remember it?

A. Yes, sir.

Q. The line from Amarillo to Wichita, that, as I understand, when it was built, was built for the purpose of taking care of the demand you had for gas at that time?

A. Yes, sir.

Q. You already had the demand for gas, and the Amarillo line was put in for the purpose of taking care of the demand at that time, that had already accumulated?

A. To take care of it, based on the disappearing supply with which we had previously been taking care of it.

Q. I understand that, but the Oklahoma line was built [fol. 525] to take care of a demand that you then had for gas?

A. Yes, it was with the idea of supplying ourselves with gas at a cheaper price than we had been forced to pay, otherwise, before this field came in.

Q. You already had the demand for the gas?

A. Yes, and we already had a source of supply, but this was a cheaper source.

Q. Where is your large demand for domestic use, Mr. Hamilton, the two Kansas Cities?

A. The two Kansas Cities.

Q. Of course, you have had these two Kansas Cities for a long time?

A. Yes, sir.

Q. And the demand there on account of the industrial gas, you have been furnishing, has been becoming larger in the last three or four years?

A. No, because the only thing we consider in the demand is our peak demand—that is the thing that bothers us. What has been happening is the domestic consumers when we bought the plant were using gas on a basis of some 40,000 feet and now they are using 67,000, as I remember it.

Q. When you bought it what was the industrial demand?

A. There was none.

Q. What is it now?

A. It is very large now.

Q. It is considerably more in thousand cubic feet than the domestic, is it not?

A. Not than the maximum domestic, no. In the summer time it is very much more.

Q. The total amount of gas furnished per year in Kansas City, for industrial, how does it compare with the total amount furnished in Kansas City for domestic?

A. I cannot tell you that offhand.

Q. Is it more, or less?

A. I cannot tell you that, even. I can find out, very easily.

Q. Do you have it in the exhibits that have been furnished?

A. I think it is one of these exhibits, but I don't know whether it is segregated as to Kansas City or not.

Mr. Stone: It is in the earnings statement.

The Witness: Kansas City Gas Company, the domestic sales here for the year ending June 30, 1931, were 7,985,826 M. cubic feet, and the industrial sales were 7,070,343 M. cubic feet. In other words, the industrial sales are about eleven or twelve per cent less than the domestic sales.

Q. What was it for the year ending December 31st?

A. For December 31st, 1930, the domestic was 7,410,603 M. cubic feet, just about ten per cent more in industrial than domestic.

Q. When was it you first took on the furnishing of industrial gas in the Kansas Cities, Mr. Hamilton?

A. I don't believe I can tell you that. It was some time ago, however.

Q. You cannot tell us the date?

A. No, I cannot, because I am not familiar with the operations except in a general way.

Q. How many lines do you have into Kansas City?

A. Three.

[fol. 326] Q. One of those was built rather recently, Mr. Hamilton?

A. I don't know the date of it. I know it was rather recently but I cannot tell you the date.

Q. That was an additional line to take care of increased capacity there, at Kansas City?

A. Yes, it was. * * *

"Hamilton further testified, on cross-examination (T. 1572-1574), as follows:

"* * * Q. Do you mean to say, Mr. Hamilton, that every plant of the same value should have the same allowance for going value?

A. No, because there would be a very different allowance between your pipe line plant or your distribution plant or an electric plant, or something like that, there might be a wholly different basis.

Q. For instance you take the distribution plant, take the one herein Topeka, for example——

A. Yes, sir.

Q. If you assumed that you would reproduce it now, and it had no customers, it would mean you would have to attach in that case, thousands of customers before the business was established?

A. That is true, and ten per cent allowance in that distribution plant would not be sufficient, in my judgment.

Q. Then take a pipe line company like this, and the number of customers you have is not very large, very many involved, don't exceed three or four hundred?

A. That is true.

Q. That should be taken into consideration in arriving at the going value in this case?

A. That is true.

Q. Then I take it you should take into consideration the fact here that the towns supplied by this pipe line company, with the exception of perhaps Superior, Nebraska, and those on that line west are accustomed to using natural gas. Kansas City, Topeka, Wichita, Ottawa, and towns of that kind have used natural gas for years, isn't that true?

A. That is what makes this pipe line valuable, because they have used it, and are in the habit of using it, and don't want to use anything else.

Q. And you should take into consideration that the building of this pipe line to those towns, those towns that already have been educated to be using natural gas?

A. You should not take it into consideration when you are arriving at a going concern value, no, sir, because that is what makes the going concern value.

Q. Well, if it does make it it should be taken into consideration?

A. Yes, sir.

Q. I thought you said it should not be.

A. It should not be to reduce it, because it makes the going value.

Q. You mean to say it should not be taken into consideration to make it less?

A. I make a distinction between that and a town which has not been using gas, after you get it up to normal consumption.

Q. Then I understand in arriving at this going value, when you furnish gas to a distributing company that is in a town that has never used gas before, you say in cases of that kind there is a period of time before the people will be educated to using gas, and therefore if they are now educated to using gas, your going value should be that much more, is that the idea?

[fol. 527] A. No, it should be the same in both towns after they get up to the normal use of gas. Now at the time the pipe line is first constructed to new towns that have not used gas, its going value would be less during those years, while they were getting up and getting into that condition of carrying the full load.

Q. The cost of attaching the business, if you supply that gas to a company in a town where they are already educated to taking gas, it would not take so long there, and the expenses of acquiring the business would not be near as much?

A. If you could presuppose some other pipe line had been supplying this town with gas, and today they could cut off and tomorrow we go in, it wouldn't take any time, but that isn't the conditions under which pipe lines are built. * * *"

"Jarboe, superintendent of all pipe lines of the system, testified that the line to the Amarillo field was constructed for the purpose of taking care of the present demand of the pipe line system.

"Hamilton testified on cross-examination:

'Q. The line from Amarillo to Wichita, that as I understand, when it was built was built for the purpose of taking care of the demand for gas you had at that time?

'A. Yes, sir.'

"Hamilton on redirect examination testified as follows (T. 1563-1574):

"* * * Q. Would you say there was an element of value to a pipe line system such as the Cities Service Gas Company in having the distributing companies in its major

markets associated with it so that its markets were sure to continue to the pipe line company?

A. There is a value in that, of course. There is not only a value in that factor, but there is also a value in the harmonious working with the distributing company in the handling of your load.

Q. Is it not true that these distributing companies were purchased by Cities Service Gas Company for the reason that it considered it necessary to have a harmonious working agreement between pipe line company and the distributing company?

A. That was one of the reasons, the other was to get better practice in the distributing companies from an engineering and operating standpoint.

Q. Those distributing companies when purchased were all losing money, were they not?

A. Practically all of them. None of them were making a fair return.

Q. Isn't that an element that enters into the going value you have used, the fact that these companies are associated, their practices have been controlled, and their business built up in the manner it has been?

A. That is perfectly true.

Q. When a pipe line is built to a town that has not had gas before, is it true that the business comes to the distributing company immediately, or does it take a period of time to attach that business?

A. It takes a period of time and a lot of expenditure of effort to get it.

Q. The pipe line from Hutchinson to Superior, Nebraska, which has been built about a year, that pipe line is not at this time making a return at all, is it?

A. Oh, no.

[fol. 528] Q. And it won't be for a number of years, takes time to build up that business?

A. That is perfectly true, and even when you build it, as we did, renewed a line to St. Joe, where they had previously had natural gas and then had used artificial gas for a few years there, the consumption is not near, and won't be for some time, up to what we finally expect to get it, and not up to the figures for which the pipe line was designed originally.

Q. The acquisition of the Kansas City Company was referred to. I will ask you if prior to the acquisition of that company by the Cities Service group, the relations between the pipe line company and the distributing company were friendly or unfriendly?

A. They were unfriendly.

Q. There had been considerable litigation between the two companies, had there not?

A. Almost endless.

Q. I will ask you whether you have any information in regard to the Chicago pipe line, as to whether any cities were attached to that line or any gas put through it prior to the time the line as a whole was constructed?

A. No gas except for testing purposes.

Q. So that line was not completed part way and then put in operation as to a part of the total market, but was entirely completed before it was utilized in any respect?

A. That is true.

Q. Are you certain as to the fourteen months you testified to that it took to construct that line? Wasn't a considerably greater period, all of two summers and one winter?

A. I am talking about the actual time of construction.

Q. Well, if you don't know, I don't want you to guess at it, but I think you are in error about it. In that job, and in any other similar job it would be necessary to order the pipe a long time——

A. I am not talking about time for design of the pipe line, or time spent working our contracts, or anything except the actual construction work out on the job.

Q. Well, buying pipe would be a part of the construction period, wouldn't it?

A. It would be part of that period, but not part of the construction work. I was referring to the actual time that we — spending money out on the job.

Q. There is no pipe on hand for a project such as the Chicago line, or this system, to be purchased, is there? That is, there is no pipe in stock?

A. Not such quantities as that, no, very small amount of pipe in stock.

Q. Has to be made specially by the mile, to fit the project?

A. In the Chicago line it was not only made, but there was nearly two years spent in the design of the pipe itself, and getting the pipe mills up to the point where they would make the pipe to withstand the pressures that were demanded.

Q. It was even necessary in some cases, was it not, for pipe manufacturers to build new mills to manufacture that pipe?

A. That was true, but away back of that was at least three years of time spent in getting the mills to even believe they could build the type of pipe we wanted.

Mr. Garver: I believe that is all.

Recross-examination.

Questions by Mr. Welch:

[fol. 529] Q. You say that you think it is more value to your company to be furnishing this gas to affiliated companies like the Kansas City, where they are controlled by the same company?

A. I think unless they should be controlled by another large holding company with ample facilities to go ahead and do the job as well as we think we can do it; in other words, at a time like this, if you had a small, isolated company to which you were supplying gas, and there was a question of extensions, it might not be able to raise the money.

Q. You are more friendly to the pipe line company than a foreign company would be?

A. No, a foreign company, if it is a large operating company, but an individual small company is often pressed by their necessities into an attitude that might not be to the best business principles.

Q. Isn't it true it would be more liable to pay you a little more for gas than it could get it for from some one else, if it is true the distribution company is owned by the same companies the pipe line companies are owned, wouldn't it be inclined to pay you a little bit higher price for gas than it could get it from someone else?

A. In the sense that they would not take up with a temporary supply and feel they could not get a permanent supply. Very naturally, since the preferred stocks are owned

by different companies that would have to do the best they could for themselves, we could not get ourselves in the position of penalizing the Kansas City Gas Company, for instance, with several millions of stocks and bonds owned by other people than ourselves, for the benefit of a company they only owned the common.

Q. I asked you whether you didn't think it would be inclined to take gas from you and pay you a higher rate than they could get gas from some other company.

A. No, I think they would be inclined to take gas from us on an equal basis.

Q. Now with reference to this pipe. you don't have to pay for the pipe when it is delivered, I take it that you pay for construction of the line?

A. That is true.

Q. So the fact that you had ordered your pipe sometime before the line was actually constructed, your cost of financing would not commence so far as your pipe was concerned, until you got your pipe.

A. No, that is perfectly true, but I was referring to cost of engineering and that sort of work that has to be done prior to placing orders.

Q. This preliminary engineering, of course, would have to be done in order to determine how much pipe you had?

A. That is true.

Q. I take it that is about the first thing you would do when you organized your concern, see whether it is feasible?

A. Yes, sir.

Q. And after that was done and you determined how much pipe you then ordered the pipe, it would be delivered, I suppose, as manufactured?

A. That is the way it was delivered.

Q. You would not have to wait for all the pipe for the system to be completed at the mill before you commenced construction of the plant?

A. No, you would not.

[fol. 530] Q. They would go ahead and manufacture a certain amount of it, and make delivery to you, probably make delivery to you as you needed it?

A. That is true, and the thing I had in the back of my head when I said fourteen months, I do not know that they averaged for that fourteen months, an expenditure of a

million dollars a week. That is what I had in mind, we were spending that money.

Q. You say we, who you mean?

A. I mean Henry L. Doherty & Company's people, because we were in the partnerships appointed to construct and have since been appointed to operate the line for the various partners in it.

Q. You are referring, then, to the construction of this Texhoma line to Chicago?

A. Yes, sir.

Mr. Garver:

Q. Mr. Hamilton, the practices of recognized engineers in valuing property have become very largely standardized, have they not?

A. To a very considerable degree, yes.

Mr. Garver: Properties have been valued for years for rate cases, and certain practices have developed?

A. Yes, sir.

Mr. Garver: Which are recognized, and there have been innumerable court decisions in regard to allowances for working capital, and going value?

A. Yes.

Mr. Garver: All those overhead items that you have used, have there not?

A. That is true.

Mr. Garver: Are the percentages which you have used in conformity with the generally recognized practice of engineers in valuing properties?

A. I should say so.

Mr. Garver: And with the decisions of the courts and commissions, generally?

A. Yes, sir.

By Mr. Welch:

Q. At any rate you think they are in accordance with the decisions of the courts?

A. I think that based on the cases in which I have been testifying, and in which the allowance have been made.

Q. Do you mean to say, Mr. Hamilton, that every plant of the same value should have the same allowance for going value?

A. No, because there would be a very different allowance between your pipe line plant or your distribution plant or an electric plant, or something like that, there might be a wholly different basis.

Q. For instance you take the distribution plant, take the one here in Topeka, for example——

A. Yes, sir.

Q. If you assumed that you would reproduce it now, and it had no customers, it would mean you would have to attach in that case, thousands of customers before the business was established?

A. That is true, and ten per cent allowance in that distribution plant would not be sufficient, in my judgment.

Q. Then take a pipe line company like this, and the number of customers you have is not very large, very many involved, don't exceed three or four hundred?

A. That is true.

[fol. 531] Q. That should be taken into consideration in arriving at the going value in this case?

A. That is true.

Q. Then I take it you should take into consideration the fact here that the towns supplied by this pipe line company, with the exception of perhaps Superior, Nebraska, and those on the line west are accustomed to using natural gas, Kansas City, Topeka, Wichita, Ottawa, and towns of that kind have used natural gas for years, isn't that true?

A. That is what makes this pipe line valuable, because they have used it, and are in the habit of using it, and don't want to use anything else.

Q. And you should take into consideration that the building of this pipe line to those towns, those towns that already have been educated to be using natural gas?

A. You should not take it into consideration when you are arriving at a going concern value, no, sir, because that is what makes the going concern value.

Q. Well, if it does make it it should be taken into consideration?

A. Yes, sir.

Q. I thought you said it should not be?

A. It should not be to reduce it, because it makes the going value.

Q. Q. You mean to say it should not be taken into consideration to make it less?

A. I make a distinction between that and a town which had not been using gas, after you get it up to normal consumption.

Q. Then I understand in arriving at this going value, when you furnish gas to a distributing company that is in a town that has never used gas before, you say in cases of that kind there is a period of time before the people will be educated to using gas, and therefore if they are now educated to using gas, your going value should be that much more, is that the idea?

A. No, it should be the same in both towns after they get up to the normal use of gas. Now at the time the pipe line is first constructed to new towns that have not used gas, its going value would be less during those years, while they were getting up and getting into that condition of carrying the full load.

Q. The cost of attaching the business, if you supplied that gas to a company in a town where they are already educated to taking gas, it would not take so long there, and the expense of acquiring the business would not be near as much?

A. If you could presuppose some other pipe line had been supplying this town with gas, and today they could cut off and tomorrow we go on, it wouldn't take any time, but that isn't the conditions under which pipe lines are built. * * *"

"Eastman testified as to the Amarillo line from Texas to Wichita and Ottawa:

'Q. Now this line was built to Texas, was any addition to the market procured from that line, were any additional markets procured, any new customers? Are there any connected to that line between Texas and Wichita?

'A. No new cities, there may be a few small towns along that main line served, but they are inconsequential.

'Q. Was there any other purpose than to supply existing markets?

'A. No.'

"Eastman testified that the line from Ottawa to Kansas City was finished in 1929.

[fol. 532] "In January, 1930, from the 18th to the 19th, the pipeline's capacity was exceeded and it was necessary to shut off the industrial gas in order to supply the demand for domestic gas.

"Hamilton testified the third line was built from Ottawa to Kansas City to take care — increased capacity there.

"Jarboe testified further that the lines to the Amarillo, Oklahoma City and Seminole fields are purely extensions to procure additional supply. No new customers were added, just went to take care of the market.

"At the time of the purchase of the Kansas Natural, the personnel was retained and continued their work. There was a demand for the gas line from Wichita to Texas, the Amarillo line. The same is true with reference to all the additions put on to the old system.

'Q. As I understand it each one of them was built because there was a need and it was necessary to complete this, to furnish gas to the main pipe line, or to places where it had already contracted or made arrangements to sell gas?

A. One or the other.

Q. That is correct?

A. Yes.

Q. Each one of those red lines denoting the construction of new pipe lines was built by the Cities Service in order to fill a need that existed at that time?

A. Yes.

Q. Upon their being completed they were then immediately put in use?

A. Yes.

Q. And have been in use and operation since then?

A. Yes.'"

[fol. 533] Gas Leases

The following agreed statement was submitted to the District Court as evidence pertaining to Gas Leases:

"The company owned as of September 1, 1931, gas leases covering 1,262,361 acres of land situated in Kansas, Oklahoma, Missouri and Texas.

"These leases grant to the lessee the right to drill for and take oil and gas, and generally (with some exceptions), run for a period of ten years from date, after which, if oil or gas is not then being produced they expire, otherwise they run so long as oil or gas is produced. The leases in general require the payment of rental until development and require the lessee, after development, to pay to lessors a royalty of one-eighth of the oil and gas. The Company

owns only the gas rights in these leases, the oil rights being held in most cases by affiliated companies.

"These leases have been classified into developed, proven, probable and prospective.

" 'Developed' leases are those on which gas is actually being produced.

" 'Proven' are those adjacent to production, which will be drilled and on which it is considered gas will be found.

" 'Probable' consists of acreage adjacent to proven acreage having favorable geological structure, but which has not been completely tested.

" 'Prospective' consist of all other acreage.

" 'The acreage owned by the company, and appellee's classification of them is as follows (Ex. 40):

[fol. 534]	Developed	Proven	Probable	Prospective, A	Total
Texas	22,690	73,730	24,547	.....	119,367
Hugoton (Kan. & Okla.)	.....	123,440	.....	.....	123,440
Okla., Kan. & Mo.	20,207	.....	1,060	.....	21,267
Okla., Kan. & Texas	.....	.....	.....	998,287	998,287
	42,297	196,170	25,607	998,287	1,262,361

"The same leases (excluding the Kansas, Oklahoma and Missouri, proven and probable) are classified by F. G. Holl, for the Commission, as follows:

Amarillo Field

Proved Area:	Acres	
Blocked	60,940	
Unblocked	33,767	
Total		94,707

Hugoton Field

Proved Area:	Acres	
Blocked	25,280	
Unblocked	59,087	
Total	84,367	
Probable or semi-proved areas	32,008	
Total	116,375	116,375

Kansas, Oklahoma, Texas and Missouri.

	Acres	
Favorable Acreage:		
Kansas	132,202	
Oklahoma	91,317	
Texas	36,326	
Missouri	9,064	
Total		268,909
Prospective Acreage:		
Kansas	364,669	
Oklahoma	248,208	
Texas	3,203	
Total		616,073
No value for gas:		
Texas	10,569	
Oklahoma	26,408	
Kansas	80,090	
Total		117,094
Grand Total		1,223,178

[fol. 335] Appellees contend that the fair value of these leases, exclusive of the wells and equipment, is $12,914,189.00, as follows:

All Cities Service Gas Company Acreage Average Value Shown by Appellee's Witnesses

Name of field	Acres proven	Acres probable	Acres prospective	Total	Value per acre.
Amarillo	94,820			$8,879,628	$93.64 plus
		24,547		422,367	17.20 plus
Hugoton	123,440			1,172,680	9.50
All other	20,207			377,940	10.70 plus
		1,060		65,000	61.32 plus
			908,287	1,996,574	2.00
Grand total	238,867	25,607	908,287	$12,914,189	

[fol. 336] The several witnesses for the Company testifying as to the present fair market value of leases with respect to their experience and qualifications testified as follows:

J. N. Nisbet: That he is Chief Geologist of the Empire Companies including the Cities Service Gas Company; that he graduated from Leland Stanford University in

1916; that since 1916 he has had experience as a geologist over the entire mid-continent area particularly in Kansas, Oklahoma, Texas, Louisiana, Arkansas and New Mexico; that he has occupied his present position a little less than three years; that he is generally familiar with the prices that have been paid for leases in the Amarillo Field during the last five or ten years; that he is familiar with the present market value of acreage in that locality; that the prices testified to by him are not figured on the amount of gas under the ground and the market for such gas but what the present market is for the several leases; that his testimony is based on the study he has made of the field and his knowledge of exchanges and sales that have actually taken place; that he is familiar with the transactions that have taken place in the Hugoton Field and with the present market value of acreage in that field; that he is familiar with the present market value of acreage such as is owned by the company outside of the Amarillo and Hugoton Field.

Richard T. Lyons: That he is Vice President of the Skelley Oil Company and in charge of the Division of Lands and Leases; that he has occupied that position slightly over two years; that he has had twelve years' experience in the oil and gas business prior to the last two years; that he has supervised all lease purchases and sales by the Skelley Oil Company in the last two years; that his company has purchased and sold leases in the Amarillo Field during the last two years; that he is familiar with some of the transactions in the purchase and sale of leases [fol. 537] in that field in the last two years; that he is familiar with the present market value of leases in the Amarillo Field; that he is familiar with the present market value of leases in the Hugoton Field; that his company has bought acreage in that field; that his company owns acreage scattered all over the Amarillo Field comprising approximately 50,000 acres; that his company also owns acreage in the Hugoton Field, practically all of which was acquired in April, May and June of 1930.

B. A. Hardey: That he is an oil and gas operator connected with Moody Seagraves interests and Vice-President

of several of their companies; that he is familiar with the Hugoton Gas Field since April, 1929; that companies with which he is connected own approximately 450,000 acres of leases in that field; that all of this acreage was purchased since April, 1929, and that he is familiar with these purchases as all leases were taken either by him personally or under his supervision; that he follows rather carefully the transactions of all other companies in that field; that he is familiar with the present fair market value of leases in that field; that his testimony as to present market prices is based on his own purchases and observations of purchases made by others.

J. D. FREEMAN: That he is in charge of the geological and land and lease work for the Panhandle Eastern Pipe Line Company; that he is an engineer and not a geologist; that he has been in the gas business since 1903; that he is familiar with the Amarillo Gas Field; that he is familiar with purchases and sales that have taken place in that field in the last few years and under his direction purchased acreage for his company; that his company has about 70,000 acres in the Amarillo field; that the last leases he purchased were in March and April, 1931.

[fol. 538] A. W. LEONARD: That he is Vice-President of the Panhandle Eastern Pipe Line Company and has had thirty-five years' experience in the gas business; that he is neither an engineer or a geologist but connected with the Operating Department; that he went with his present company in October, 1930; that he is familiar with the purchases of gas acreage made by his company in the Amarillo Field, the last of which was purchased in August and September, 1930.

STANLEY MARSH: That he trades in oil and gas leases and oil and gas properties, his office being in Amarillo, Texas; that he has been acquainted with the Amarillo Field five years and has been engaged in the lease brokerage business in that field for four or five years; that he is familiar with most of the transactions that have taken place in the field; that he is familiar with the present market value of leases in the Amarillo Field.

VICTOR A. HAYES: That he has spent over thirty years in the natural gas business and has been associated with many different companies; that he has been familiar with the Amarillo Gas Field since 1924 and watched it from the beginning; that for the past four and a half years he was General Manager for the Southwestern Development Company and purchased their large holdings of acreage in that field; that he is familiar with the present market value of gas acreage in that field; that the last purchases he made were within six or eight months, the purchase consisting of 2,700 acres.

R. J. WALLACE: That he is in the brokerage business at Tulsa, Oklahoma, and has been for about six years; that in connection with his business he has kept himself informed as to the value of acreage in the Amarillo Field and is familiar with present market values.

[fol. 539] ROSS M. STUNTZ: That he is Superintendent of Gas Production for the Cities Service Gas Company; that he has been in the gas business practically all of the time since 1905; that all gas purchase contracts for the Cities Service Gas Company pass through his Department and are subject to his supervision and that he is familiar with the prices paid by the Cities Service Gas Company for all gas leases held by it and with sales and exchanges that have taken place in the several fields within recent years.

R. E. DAVIS: That he lives in Pittsburgh, Pennsylvania, and is a Consulting Geological Engineer; that his principal office is in Pittsburgh with some offices in New York, Charleston, West Virginia, and Shreveport, Louisiana; that he has been in such business twenty-five years; that all of his time for the last twenty-five years has been given to oil and gas work; that his firm has examined one or several times every important gas field in the country; that quite a large part of his work has been done for operating companies; that this is his first employment by any of the parties to this suit; that he was not employed to price the gas reserves of the Cities Service Gas Company but to value them; that his estimate is that of intrinsic value and not market price; that he determined his value in the same manner as if he were

employed by a client who was contemplating buying or a banker desiring to approve securities.

Davis testified that he did not attempt to ascertain market values or attempt to price the gas reserves of the Cities Service Gas Company in that manner but made a valuation by computing the amount of gas in reserve in accordance with the recognized practices of the industry and testified that, in his opinion, the value of the gas reserves, as a whole, was $20,588,000.00, including wells, the witness further testi- [fol. 540] fied that if the value of gas reserves, exclusive of wells, is to be determined the value found for the wells should be excluded from the above figure. (In Finding 14 the Court found the value of these wells to be $1,953,149.00 which would leave the value of the gas reserves, as testified to by Davis, $18,634,851.00).

Davis testified that in making his valuation he followed exactly the same procedure as if he were employed by any other client such as a banker or prospective purchaser and that the value testified to by him was the value he would use in such case.

Davis testified that he arrived at the intrinsic value of the proven and probable leases included in the above valuation by calculating the volume of the recoverable gas from these leases, and multiplying this by his estimated prices per 1000 c. f. of gas at the mouth of the well.

The testimony of these witnesses as to the present fair market value of the gas leases of the Cities Service Gas Company is set out in Exhibit 40, as follows:

[fol. 541]

All Cities Service Gas Company Acreage

Average market value as testified

Name of field	Proven		Probable		Prospective		Grand totals	
	Acres	Value	Acres	Value	Acres	Value	Acres	Value
Amarillo	94,820	8,879,628	24,547	422,367			119,367	9,301,995
Hugoton	123,440	1,172,680					123,440	1,172,680
All Other	20,207	377,940	1,060	65,000	998,287	1,996,574	1,019,554	2,439,514
Grand total	238,467	10,430,248	25,607	487,367	998,287	1,996,574	1,262,361	13,914,189

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Estimate Book

Tenancy of		Present				Previous			
		Page	Acres	Price	Value	Page	Acres	Price	Value
J. M. Nisbet		387	34 2251	100	£ 992 100	271	11 1491	25	365 100
A. W. Tennant	Blocked	388	10 2251	100	£ 1 100	273	34 2251	25	862 100
	Scattered	388	6 1000	45	257 100	273			
	Total		34 2251		£ 1259 100				
J. D. Freeman	Blocked	390	10 2251	100	£ 1 100	390	23 2251	24	565 100
	Scattered	390	6 1000	57	342 100				
			34 2251		£ 1259 100				
R. T. Lyons		434	34 2251	75	£ 1 100				
Stanley March	Blocked	437	32 3000	225	£ 1 100	440	1 1000	22	25 100
	Scattered	437	2 1000	75	1 100				
		437	34 3251	45	127 100				
	Total		34 2251		£ 1 100				
Victor A. Hayes	Blocked	341	10 2251	100	£ 1 100				
	Tenant's average		6 1000		258 125				
	Total		34 2251		£ 1 125				
R. J. Wallace	Blocked	392	10 2251	100	£ 1 100	392	11 1491	13	145 100
	Scattered	392	6 1000	75	345 100				
	Total		34 2251		£ 1 100				
R. M. Stuntz	Blocked	393	10 2251	100	£ 1 100	393	34 3501	11	145 100
	Scattered		6 1000	50	258 100				
	Total		34 2251		£ 1 100				
Grand Total					£ 137 125				
Average Total			34 2251		£ 1 129		34 3457		£ 1
Average per Acre					18 4				

[fol. 548]

Hugoton Field

Testimony of	Page	Acres	Proven Price	Value
J. M. Nesbit	369	123,440	10.00	1,234,400.00
B. A. Hardy	472	123,440	10.00	1,234,400.00
J. D. Freeman	601	123,440	10.00	1,234,400.00
R. T. Lyons	635	123,440	8.00	987,520.00
Average Total				1,172,680.00
Average per acre				9.50

[fol. 544]

All Other Fields

	Proven				Probable				Prospective			
Testimony of	Page	Acres	Price	Value	Page	Acres	Price	Value	Page	Acres	Price	Value
J. M. Nesbit	....								379	1,005,194	2.00	2,010,388.00
R. T. Lyons	....								427	1,005,194	2.00	2,010,388.00
R. M. Stuntz												
Kansas	917	16,125		139,240.00								
Okla. & Mo.	917-9	4,082		239,700								
Total	....	20,207		377,940	935	1,000		15,000.00				

[fol. 545] Computation for Prospective Acreage

Total Proven Amarillo	94820	
Total Probable Amarillo	24547	
Total Proven Hugoton	123440	
Total Proven all other fields	20207	
Total Probable all other fields	1060	
Total	264074	
Prospective	998287 Acres @ 2.00	$1,996,574.00
Grand Total	1262361	

[fol. 546] "These witnesses varied in their opinions of value of different tracts, the average of their testimony as to the present fair market value of all acreage being $12,914,189.00.

"The only witness testifying for the Public Service Commission was F. G. Holl, employed by it to value the gas leases of the Cities Service Gas Company, who testified as to his experience and qualifications as follows:

Direct examination:

"'A. Since January, 1919, I have devoted all of my time to the oil and gas business in varying activities. I commenced as a roustabout on a lease, dressed tools, and after about a year I was employed by the Empire Gas & Fuel Company in their geological department. My employment with them lasted over a period of almost six years. During more than a year of that time I was resident geologist for that company at Duncan, Oklahoma, and during the last three and a half years of that time I was resident geologist for the company at Eldorado, Kansas. As resident geologist, my work had to do with location of wells, drilling well, collection of data, and samples, geological work relating to these activities to some extent, examination of wildcat territory, recommendations on acquisition of acreage, and on rental payments. After leaving the Empire Company, in April of 1923, I was employed by the Ramsey Petroleum Company, of Eldorado, Kansas, for a period of one year. During that time, as their geologist, my work had to do with exploration, and during that period the Company acquired acreage and drilled wells and since April, 1926, I have been a consulting geologist and independent operator.' In P. 1878.

"I have bought, sold and developed oil and gas leases. I am familiar with the Amarillo and Hugoton fields. I have personally inspected and made a study of these fields. The market price for gas in the wells in the Amarillo field is 2 cents per M. c. f. I know the fair market value of oil and gas leases, insofar as there is any market value in these fields.

Cross-examination:

That he was 34 years old, and was not a college graduate and had no scientific degree; that after leaving school where he studied some geology he was employed by the Empire Gas & Fuel Company in September, 1919, in the so-called subsurface branch of the geologist department at Oil Hill; that he worked under H. R. Shidell, resident [fol. 547] geologist who reported to A. W. McCoy, who in turn reported to L. C. Snyder, chief geologist, at Bartlesville; that he had nothing to do with the purchase of leases; that his next position was with the same company at Duncan, Oklahoma, where there was an oil and gas field; that his duties at Duncan consisted of writing recommendations as to the location of both oil and gas wells; that he was in charge of geological office at Duncan; that he had no final judgment in regard to any matters; that he was given the responsibility of determining the point at which the casing should be set on rotary drill holes; that he kept track of the log of wells and ran samples; that all he had to do with the acquistion of leases was suggestions and recommendations in his reports; that in 1922, he was transferred from Duncan to Oil Hill, Kansas, as resident geologist; that in the course of his duties he made numerous recommendations chiefly in regard to construction work; that he was sent practically all over the state to make special reports; that he never worked in the land and lease department and never purchased but one lease for the company; that it was part of his duties to suggest leases for the company to drill on and the company drilled these leases; that he occupied that position three and one-half years, after which he went with the Ramsey Petroleum Company at Eldorado; that he personally handled over three or four thousand acres of oil leases purchased for that company; that he did no gas work for that company; that he occupied that position for a year and one month and then went into private practice as a consulting geologist.

"Q. Your qualifications as a consulting geologist at the time you opened your office were such as you have related up to this time, that was your experience, was it?

"A. Yes.

"Q. Are you still in that position?

"A. Yes.

"Q. You have been employed by the state to make a survey concerning which you have testified?

"A. Yes, sir.

"Q. It was 1926 you went into the business of a consulting geologist?

"A. Yes, sir.

"Q. Have you made any valuation of gas reserves for [fol. 548] any company since 1926, in the course of your business?

"A. I have made investigations.

"Q. Did any gas company, any oil company, any investment firm, any banker or any of the usual clients of that nature ever employ you to make an investigation and appraisal or valuation of a major oil or gas pool, the acreage of it?

"A. No, sir.

"Q. Prior to the time you were employed by the state in this case, had you made any such investigation or valuation anywhere, with the idea of fixing the value of leases?

"A. No. Prior to the time—you mean producing leases?

"Q. Yes, anything similar to what you are investigating now.

"A. Well, I think that most of my work has been of a similar nature.

"Q. Of a similar nature?

"A. Yes, sir.

"Q. For whom?

"A. For myself and for indepndent operators.

"Q. For what independent operator have you ever made an appraisal or valuation of gas reserves?

"A. I have made no such.

"Q. Well, when was your first experience with the Amarillo field, Mr. Holl?

"A. Since I was employed by the state.

"Q. You had no knowledge of the field prior to that time?

"A. Only a general knowledge from the literature which I had read on it.

"Q. You had never been down there and looked it over?

"A. Had not been until that time, no, sir.

"Q. What was your first experience with the Hugoton field?

"A. Two or three years ago.

"Q. That is when it first came in?

"A. Yes, sir.

"Q. Were you interested in it in the course of your business, or did you investigate it for some one?

"A. I was out there and investigated it for myself.

"Q. Just to satisfy yourself as to what there was out there as a matter of general information?

"A. Yes, and with the view of possible investments there.

"Q. Did you make any investments there?

"A. No, sir.

"Q. You stated that you were a geologist, and independent operator. What property have you operated? I am not going to inquire into your private affairs; it is not with that idea.

"A. I am not at this time operating any producing oil or gas leases which are operated by other companies.

"Q. Have you ever operated any oil or gas leases?

"A. I have drilled wells, if that constitutes operation.

"Q. Well, you have stated in the course of your employment you had done geological work, and you have drilled wells?

"A. Yes, and on my own account I have drilled wells.

"Q. As a driller?

"A. No, as an operator.

"Q. Now as to the Amarillo field, have you any independent knowledge of any transactions that have been taking place in the purchase or sale of leases?

"A. Yes, sir.

[fol. 549] "Q. You have never handled any such transaction yourself.

"A. No, I have not.

"Q. So what you know about it is what you have been told?

"A. Yes, sir, and what I have personally investigated.

"Q. What investigation did you make in the Amarillo field as the basis of your judgment as to the value of leases in that field?

"A. I familiarized myself with the lease situation there, prepared a map such as the map Exhibit G, and saw what acreage was leased to the different companies, pipe line companies, what acreage was either open or leased to oil

companies, or independent operators, I visited all the towns and county seats in the area, talked to bankers, abstractors, lease brokers, where there were any, visited all the principal offices in the Amarillo field, the oil and gas companies, talked with their geologists, land men and scouts.

"Q. That was to determine what acreage was good and what was bad, and the probable amount of gas in reserve, I take it?

"A. I wanted the information, all the information I could get from these men who were very familiar with conditions.

"Q. Did you ask them in regard to the market value, or price of acreage there, leases?

"A. Yes, sir.

"Q. Did you talk with the broker from Amarillo who testified in this case?

"A. Mr. Marsh?

"Q. Yes.

"A. Yes, I talked with Mr. Marsh.

"Q. Did the value he gave you correspond at all with the judgment you have now expressed?

"A. No, sir.

"Q. So you did not consider his judgment in the matter, did you, at all, did you tell these men that you talked to the nature of your employment and that you were representing the state in this proceeding?

"A. Yes, sir.

"Q. You didn't pose as a prospective purchaser trying to collect acreage, at all?

"A. Not to the men in Amarillo. * * *,"

"At the close of Holl's testimony before the Commission the respondents moved to strike out all the testimony given by him as follows:

"'* * * Mr. Garver: If the Commission please, the respondents and each of them, now move to strike from the record all of the testimony of Mr. Holl, in regard to the market value of leases in the Amarillo field, for the reason that he has not qualified himself as being able to testify to those values, inasmuch as he never operated in that field, was never in the field, and has no personal knowledge of any transaction that has taken place there, and never had anything whatever to do with the field until he was hired by the Commission, or by the state, to go down there and make an investigation, by reason of which fact he could

not know any more about it than any other person the Commission might have hired to go down there and make indiscriminate inquiries from anyone he might choose to pick out as to what the present market values were, his information being necessarily entirely hearsay, and the witness personally having no knowledge whatever of the market value of any leases in the Amarillo field of that vicinity. [fol. 550] I desire also to make the same motion as to the testimony of the witness in regard to lease values in the Hugoton field.

"Chairman Greenleaf: The motion will be overruled. * * *"

"The Commission found the fair value of these leases, exclusive of wells and equipment at $6,279,237.00, as follows:

Commission's Valuation of Gas Leases

	Acres		Value per acre	Fair Market Value
Amarillo field (Texas), Developed and Proven:				
Blocked	60,940	@	$50.00	$3,047,000
Not Blocked	33,880	@	35.00	1,185,800
Total	94,820*			$4,232,800
Probable Acreage	24,547	@	2.00	49,094
Total	119,367			$4,281,894
Hugoton field (Kansas & Oklahoma), Proven:				
Blocked	25,280	@	$7.50	$189,600
Not Blocked	59,087	@	5.00	295,435
Probable	32,008	@	2.00	64,016
Total	116,375			
Prospective	7,065	@	1.00	7,065
Total	123,440			$556,116

* Of the above, 22,090 acres are developed with sixty producing wells.

Kansas, Oklahoma, and Missouri (exclusive of Hugoton):

	Acres	
Proven:		
Kansas, Oklahoma and Missouri	20,207	$377,940
Probable:		
Kansas, Oklahoma and Missouri	1,060	65,000
Total	21,267	$442,940

	Acres	
Prospective:		
All other except Hugoton	998,287	998,287
Total	1,262,361	$6,279,237

[fol. 551] "In the foregoing, the Commission adopted the value of all the Kansas and Oklahoma (exclusive of Hugoton field) proven and probable leases, 21,267 acres, as claimed by respondents, at $442,940.

"The value of all leases of the company, including the leases later sold to The Texhoma after deducting the value of leases canceled and surrendered, as shown by the books of the company, is (book value) $6,573,489.70 (Tr. C. H. Montgomery, Ex. 49).

"Of the 1,262,361 acres of gas leases owned by the Company the Commission found that only 42,297 have been drilled or developed. The remaining 1,220,064 acres are undrilled and are undeveloped."

Amarillo Field (Texas).

"The company owns gas leases covering 94,820 acres in what is known as proven sweet gas area in Texas, in the Amarillo field. This proven sweet gas area is a portion of a huge field in the Panhandle, and is approximately 130 miles long and from seven to forty miles wide. It contains approximately 1,001,785 acres.

"Of the company's acreage in this field, the Commission found that 22,090 acres are developed, having sixty gas wells thereon. The testimony of Ralph E. Davis, the company's witness, a gas engineer and geologist, who made a survey of the company's gas holdings, is that the recoverable gas (gas reserves) from these leases situated in this proven area, and comprising 94,820 acres, is 15,000,000 cubic feet per acre.

"One of these Texas leases is the Burnett lease (Ex. 48). It covers 63,880 acres, and requires a minimum payment of $50,000 per year, in advance, for ten years whether or not gas is taken from the lease. For the first two years, the royalty is one-eighth of 3 cents per M. cubic feet for all gas taken; for the next three years, one-eighth of 3½ cents [fol. 552] per M. cubic feet; for the next five years, one-eighth of 4 cents per M. cubic feet; thereafter, one-eighth

of 4 cents unless the price of gas at the well is increased, in which event the royalty is to be one-eighth of the weighted average price. The Burnett lease is not a solid block, there being within said lease other leases owned by others than the company, on which there are producing wells. Up to the present time the $50,000 annual payments required on this lease have exceeded the royalty earned on the gas taken.

"The witnesses for the company placed the market value of these leases at from $45 to $125 per acre, the higher values being placed on the Burnett ranch and blocked acreage. Eight witnesses testified for the respondents, two of them were employees, and all of the remaining, save one, were connected with gas companies.

"F. G. Holl, for the Commission, testified that the value of the blocked acreage, consisting of 60,940 acres, was $45 per acre, and that the value of the remainder of the proven leases, 33,767 acres, was $25 per acre. Holl testified that scattered leases in this field in Wheeler County in the vicinity where the largest wells in the entire field have been found, could be purchased at $5 per acre, not to the purchaser, such leases covering both the oil and gas. That in Potter County, near where the largest wells have been found, on September 14, 1931, a lease which was about to expire was renewed at $8 per acre for 5,000 acres.

"The evidence of respondents shows in 1931 the company conveyed to the Texoma Natural Gas Company (an affiliated company) 59,788 acres of leases, including the Coon ranch of approximately 25,000 acres which was blocked, 30,831 acres at the price of $45 per acre and 28,957 acres at an average of approximately $19 per acre. This acreage was all in the proven sweet gas area in the Amarillo field, and Holl testified that these leases are comparable with the proven and developed leases retained and [fol. 553] now owned by the company. The evidence also shows that these leases so sold to the Texhoma cost the company somewhat less than $15 per acre on the average.

"The books of the company also show that from January 1, 1930, to June 30, 1931, it purchased 21,158 acres of its leases in the Amarillo field in the sweet proven gas area, now valued by respondents at approximately $93 per acre, at an average cost of $12.78 per acre.

"The evidence of Mr. Holl shows that there is a large oversupply of gas developed by gas companies and independent producers in the Amarillo field, which on account of the lack of market, cannot be sold, and that gas is being sold in this field at 2 cents per M. cubic feet, at the well. That in the Amarillo proven sweet gas area there are approximately 125 "shut-in" wells drilled and capable of producing gas which cannot be sold for want of a market, and that these "shut-in" wells have an open flow of 2,260,000,000 cubic feet per day.

"That the owners of wells are able to sell only a small per cent of their gas; that the Lone Star Gas Company has a pipe line into this field connected to 65 wells, from which the runs averaged during the first six months of 1931, a little over 100 M. cubic feet per day, for which the company paid 2 cents per M. cubic feet, or a royalty of $2 per day, and for that reason operators are not drilling any more wells or acquiring any more acreage.

"The company owns 24,547 acres of gas leases in Texas situated outside of the proven sweet gas area, some of which are in the sour gas area.

"The Testimony of the witnesses for respondents as to the value of this acreage varied. Some stated that part of these are worthless; others at from $5 to $25 per acre.

"F. G. Holl, for the Commission, placed the fair market value of the gas rights in that part of this acreage which is classed as "favorable" at $1 per acre and 50 cents per [fol. 554] acre for that part which he classes as "prospective" and nothing for the remainder of the non-producing Texas acreage.

"The Commission found the value of the gas leases in the Amarillo field as follows:

Amarillo Field

Developed and proven:	Acres	Value per Acre	Fair Market Value
Blocked acreage	60,940	$50.00	$3,047,000
Not blocked	33,880	35.00	1,185,800
Total	94,820	.....	$4,232,800
Probable	24,547	2.00	49,094
Grand Total	119,367	.....	$4,281,894

Hugoton Field (Kansas and Oklahoma)

"The Company owns 123,440 acres of gas leases in the Hugoton field situated in northwestern Oklahoma and southwestern Kansas, all of which it contends are "proven".

"This is another enormous gas field estimated to comprise 1,000,000 acres of gas productive lands. Its limits are not yet defined. They can be determined only by additional drilling. Dr. Raymond C. Moore, State geologist, estimates the gas reserves in this field as sufficient to supply all of the state of Kansas, on the basis of that now used in Kansas, for a period of over 100 years (Tr. 1964, Ex. 47). There is a market for but a small portion of the developed gas in this field. Little drilling has been done, but there is sufficient drilling to demonstrate that this is a rich field of gigantic proportions.

"Of the company's acreage, F. G. Holl, for the Commission, classified 84,367 acres as "proven," 32,008 acres as "probable" and the remainder as "prospective."

"Ralph E. Davis, for respondents, gave it as his opinion, as a result of his geological survey made for respondents, that the recoverable gas from the "proven" area of this field is 10,000,000 cu. ft. per acre, and from the "probable" at 7,000,000 cu. ft. per acre.

[fol. 555] "There is no development and no wells on any of the company's acreage in the Hugoton field. The company's leases consist of one large lease, the Stonebreaker lease, covering 25,280 acres, and over 500 smaller leases. The terms of each of these 500 leases require the drilling of a well within ten years from its data, otherwise, the lease expires at the end of ten years. The company has no pipe line within ninety miles of these leases.

"Witnesses for respondents, four in number, testified that the fair market value of the gas rights in these leases which are in the proven area, is from $3 to $10 per acre, and the respondents claim that the fair market value of this 123,440 acres of leases is $1,172,680, or $9.50 per acre.

"F. G. Holl testified that leases for oil and gas could be purchased in the proven area of this field at the time of the hearing at $1 to $2 per acre; that the Derby Oil Company had within sixty to seventy days prior to his testimony,

purchased 5,947 acres of leases in this proven area at $1 per acre and that the fair market value of these leases is:

Hugoton Field

Hugoton Field

Proved area:	Acres		Per Acre	Fair Market Value
Blocked	25,289	@	$7.50	$189,600.00
Unblocked	59,087	@	4.50	88,630.50
Probable area	32,008	@	1.00	32,008.00
Prospective area	7,065	@	.50	3,532.50
Totals	123,440			$313,771.00

"The Commission found the value of the company leases in the Hugoton field to be $556,116.00, as follows:

Fair Market Value Leases—Hugoton

Fair Market Value Leases—Hugoton

	Acres		Per Acre	Fair Market Value
Proven (blocked)	25,280	@	$7.50	$189,600.00
Proven (not blocked)	59,087	@	5.00	295,435.00
Probable	32,008	@	2.00	64,016.00
Prospective	7,065	@	1.00	7,065.00
Totals	123,440			$556,116.00

[fol. 556] Kansas, Oklahoma and Missouri (Exclusive of Hugoton Field)

Proven and Probable

"Ross Stuntz, superintendent for the Company, testified that the company owned, in Kansas and Oklahoma, proven and developed and probable acreage, of the fair market value as follows:

	Acres		Fair Market Value	
Proven and developed:				
Kansas	16,125		$138,240	
Oklahoma	4,082		239,700	
Totals		20,207		$377,940
Probable acreage:				
Kansas	80		$8,000	
Oklahoma	980		57,000	
Totals		1,060		$65,000
		21,267		$442,940

"There was no other evidence as to the value of this acreage, and it was accepted by the Commission as correct.

Prospective Acreage

"This acreage is scattered throughout Texas, Oklahoma, Kansas and Missouri.

"From July 1, 1931, to October 1, 1931, the company surrendered 61,471 acres of prospective acreage.

"The acreage of the company's prospective leases, as classified by Mr. Nisbet, chief geologist for respondents, is 998,287 acres, which he values at $2 per acre,

"Ralph E. Davis, for respondents, classifies 1,031,127 acres of the company's leases as "prospective" and values them at $1 per acre.

"F. G. Holl, for the commission, classified 268,909 acres, as "favorable" and values them at $1 per acre, 616,073 acres as "prospective" at 50 cents per acre, and the remainder at no value.

"The foregoing being for the gas rights only.

"The Commission found the value of this prospective [fol. 557] acreage to be $1 per acre, or a total of $998,287.00.

Purchase Contracts and Gas Requirements

"The amount of gas produced and purchased by the company for the year ending December 31, 1930, is as follows:

Gas purchased and produced:	M. C. F.
Gas produced	34,401,978
Gas purchased	31,123,002
Residue Gas purchased	8,638,965
Total	74,163,945
Or on an average per day of (74,163,945 + 365)	203,189

"For the year ending June 30, 1932, the gas produced and purchased is as follows:

	M. C. F.
Gas produced	33,164,003
Gas purchased	14,848,685
Residue Gas purchased	6,608,886
Total	54,621,574
Or on an average per day of (54,621,574 + 365)	149,648

"This is an 8-oz. base, to reduce to a 2-lb. base, on which the measurement of the gas produced is based, this amount should be reduced by 9.2 per cent.

"The peak load of the company's gas system was on January 16, 1930. On that day the companies used 330,000 M. c. f. of gas.

"The pipe lines of the Company have no greater capacity than for this peak load.

"The Company has always purchased more gas than it produced. In 1930 it produced 46 per cent and purchased 54 per cent.

"The Company owns purchase contracts for gas on leases in the Kansas and Oklahoma fields adjacent to its pipe lines upon which are wells, the open flow production of which is 2,138,170 M. c. f. per day.

"These purchase contracts cover 782,421 acres of leases and 1,502 gas wells. The total open-flow capacity per day of the gas wells owned by the company, plus the gas to [fol. 558] which it is entitled under its purchase contracts, is: Open Flow per day:

	M. C. F.
Amarillo, 60 wells, 22,090 acres (~~Tr.~~ 449)	1,532,625
Kansas, Okla. & Missouri, 20,207 acres (Ex. 3, Table 3)	258,837
Add purchase contracts (Ex. 3, 82-96, Tables 16 and 17)	2,138,170
Total open flow (available to company)	3,929,632

"Respondents claim that the open-flow of the sixty wells in the Amarillo field is 250,000 M. c. f. less than the amount given above and if they are correct, the total open flow of gas available to the Company should be reduced to 3,679,632 M. c. f.

"The foregoing 3,929,632 M. c. f. is the open-flow capacity per day of the wells owend by the Company from 42,297 acres, all of its developed leases, plus the daily open-flow capacity of the wells situated on the leases covered by its purchase contracts.

"Witnesses testified that ordinarily the amount of gas which can be safely taken from a well is 20 percent of its open-flow capacity.

"The present maximum capacity of the company's pipe line from the Amarillo field, a 20-inch line, is 125,000 M. c. f. per day.

Reserves

"Witnesses testified that the total acres of gas leases of the Company is 1,262,361. That of these, 22,090 acres in the Amarillo field and 20,207 acres in Kansas, Oklahoma and Missouri are drilled and producing and the remainder 1,220,064 were not drilled or producing or called upon at that time to meet the company's requirements for gas.

[fol. 559] "Ralph E. Davis, geologist and gas engineer, witness for the company, who made an exhaustive study of the company's holdings, testified that the recoverable gas reserves in the company's leases in the Amarillo field is 15,000,000 cu. ft. per acre for the proven and 7,500,000 cu. ft. for the probable. In the Hugoton field, 10,000,000 cu. ft. per acre for the proven and 7,000,000 cu. ft. per acre for the probable, and stated that these figures are conservative. Davis testified that the total amount of the developed acreage of the Company was 58,922 acres of which 19,882 acres were in Kansas, Oklahoma and Missouri and 39,040 acres were in Texas.

"That the total recoverable gas from companies' holdings in the Amarillo, Hugoton and Kansas, Oklahoma and Missouri leases, proven and probable, amount to 2,488,664,000 M. c. f. as follows:

	Estimated gas reserves M cubic feet	Acreage
Kansas-Oklahoma (except Hugoton) and Missouri:		
Proven, Developed	23,858,000	19,882
Probable	9,566,000	1,020
Total	33,424,000	20,902
Hugoton Field:		
Proven	492,100,000	49,210
Probable	196,490,000	28,070
Total	688,590,000	77,280

Amarillo Field:	Estimated gas reserve M cubic feet	Acreage
Proven, Developed	585,600,000	39,040
Undeveloped	836,700,000	55,780
Total	1,422,300,000	94,820
Probable	304,350,000	40,580
Total	1,726,650,000	135,400
Grand Total	2,448,664,000	233,582

"The Commission found that of the 1,262,361 acres of gas leases owned by the Company only 71,267 acres thereof were used and useful and devoted to the public use.
[fol. 560] "That included in these leases designated as "used and useful" are all of the developed leases in Texas, and all of the developed proven and probable leases (except Hugoton) in Kansas, Oklahoma and Missouri. A list of these leases with their recoverable gas reserves as testified by Ralph E. Davis, respondents' geologist and gas expert and their fair value as found by the Commission is as follows:

Used and Useful Leases, as Found by the Commission

	Acres	Fair market value	Gas reserves M. c. f.
Kansas, Oklahoma & Missouri:			
All developed, proven and probable	21,267	$442,940	33,424,000
Texas, Amarillo Field:			
Blocked	45,830 @ $50	2,291,500	
Not blocked	4,170 @ $35	145,950	750,000,000
Totals	71,267	$2,880,390	783,424,000

Of these 71,267 acres, 42,297 are producing and 28,970 acres are not developed, as follows:

Proven Leases:	Acres
Developed:	
Texas	22,090
Kansas, Oklahoma & Missouri	20,207
Total	42,297

Undeveloped:	Acres	
Texas—proven	27,910	
Oklahoma—probable	980	
Kansas—probable	80	
Total	28,970	
Grand Total		71,267

"The gas reserve in these 71,267 acres according to respondent's testimony is 783,424,000 M. c. f.

"No witness testified that the leases other than the 71,267 acres were not used and useful.

"Respondents claim that all of the 1,262,361 acres of gas leases are used or useful.

[fol. 561] "The Commission found that only 71,267 acres of these leases are used and useful and rejects 1,191,094 acres as not devoted to the public use.

"Appellees value the 1,262,361 acres of leases at $12,914,189, exclusive of wells and equipment. The Commission valued these leases at $6,279,237—a difference of $6,634,952.

"Appellees value the 71,267 acres which the Commission found to be devoted to the public use at $5,124,940.

"The Commission values these leases at $2,874,390—a difference of $2,250,550.

It was agreed before the district court that the witness, F. G. Holl for the Commission, would testify "that he is familiar with the gas holdings of The City Service Gas Company, that he has made a study of them by inspection and by examination of the maps and data furnished by the Company and that he is familiar with the location of all wells owned by the Company in the Amarillo field. That he has made a calculation for the purpose of determing the amount of developed acreage owned by The City Service Gas Company as of September 1, 1931, and that in doing so he has used the following basis:

"In the case of scattered acreage he has considered that the wells situated on such scattered acreage develop the entire acreage owned by The City Service Gas Company surrounding said wells. In the case of blocked acreage he has assigned to one well, 640 acres surrounding said well, subtracting overlapping acreage due to the close spacing of wells. That from an examination of the maps furnished

by the Company showing location of wells and acreage owned, he has determined that the amount of scattered acreage, that is acreage that is not blocked, in the Amarillo field is 10,110 acres having 39 wells thereon, and that the blocked acreage is 11,980 acres, having 21 wells thereon, and that through this calculation he finds that the total developed [fol. 562] acreage of The City Service Gas Company in the Amarillo field is 22,090 acres.

"That in arriving at the developed acreage situated in Kansas and Oklahoma, he has accepted the classifications of Ralph E. Davis, geologist introduced as a witness for the company, and his written report classifying said acreage being Exhibit #3, page 36. That according to this classification, the remainder of all of the developed acreage of The City Service Gas Company is 19,882 acres. That including the developed acreage outside of the Amarillo field with that in the Amarillo field, the total developed acreage of The City Service Gas Company, as of September 1, 1931, is 41,972 acres.

"That the total number of wells owned by the City Service Gas Company as of September 1, 1931, is as follows:

Amarillo field	60
Kansas & Oklahoma producing	147
Storage	66
Dead	31
Total wells	304

"That in accordance with the records of the Railroad Commission of the State of Texas, there are at the present time in the so-called West Panhandle (Amarillo) field, 56 gas wells which are shut in and have no market for their gas. These wells have an open flow per day of 1,467,600,000 cubic feet and are situated within from one-fourth mile to five miles of The City Service line, 19 of them being within one mile of the City Service line.

"That during the year, 1932, a new field of gas has been opened in Reno County, Kansas, within approximately 28 miles from Wichita, Kansas, and 12 miles from Hutchison, Kansas, and within 3 miles of The City Service 10-inch line. That the open flow capacity of these wells at the present time is approximately 270,000,000 cubic feet per day. That

the limits of the field are not yet determined. That the City Service pipe line has recently been connected with two [fol. 563] of the wells in this field whose open flow capacity is approximately 146,000,000 cubic feet of gas per day.

"It is contended by the Complainants that the 270,000,000 cubic feet above mentioned is sour or sulphur gas and not yet proven to be useable by The Cities Service Gas Company.

"It is agreed that the book value of the leases of the Company, after deducting the cost of the leases transferred to the Texoma, is $5,727,272.00.

"Exhibit 3, pp. 20-26, prepared by Ralph E. Davis, for the Company, shows that on July 1, 1931, the Company had 147 producing gas wells and 66 storage and 31 dead wells on 19,882 acres of leases in Kansas and Oklahoma, and 60 producing wells in the Amarillo Texas field. Said Exhibit 3, Table 10, shows the amount of gas produced and purchased in M cubic feet on an 8 oz. pressure basis for the years 1927 to 1930 and six months of the year, 1931, as follows:

Cities Service Gas Company, Cities Service Gas Pipe Line Company, American Pipe Line Company

Gas Produced and Purchased

M Cubic Feet—8 oz. Pressure Base

		Kansas	Missouri	Oklahoma	Texas	Total
1927	Gas Produced	525.809		2.286.173		2.811.982
	Gas Purchased	8.386.761		19.268.498		27.655.259
	Residue Gas	737.878		14.345.453		15.083.331
	Total	9.650.448		35.900.124		45.550.572
1928	Gas Produced	1.615.217		3.694.818	10.272.560	15.582.596
	Gas Purchased	7.423.485	409.829	18.671.840	15.121	26.520.275
	Residue Gas	1.445.867		12.962.828		14.[illegible].696
	Total	10.484.569	409.829	35.319.486	10.287.681	56.501.565
1929	Gas Produced	1.343.788	6.643	4.564.662	28.230.126	34.145.219
	Gas Purchased	8.687.833	989.257	19.332.388	913.063	29.922.541
	Residue Gas	360.381		7.871.587		8.231.968
[fol. 564]	Total	10.392.002	996.900	31.768.637	29.143.189	71.299.728
1930	Gas Produced	1.054.074	10.847	3.548.557	29.788.500	34.401.978
	Gas Purchased	9.787.394	642.565	20.357.803	335.240	31.123.002
	Residue Gas	155.516		8.483.449		8.638.965
	Total	10.996.984	653.412	32.389.809	30.123.740	74.163.945
1931	Gas Produced	585.186	4.158	839.254	15.153.456	16.582.054
6 Mo.,	Gas Purchased	4.430.386	206.255	6.390.835	220.185	11.247.661
	Residue Gas	131.083		6.586.581		6.717.664
	Total	5.146.655	210.413	13.816.670	15.373.641	34.547.379

RALPH E. DAVIS, Gas Engineer and witness for the Company, testified:

In the Amarillo field the developed acreage is that part of the proven acreage surrounding the various wells that have been drilled by the Company and I have arbitrarily assigned 640 acres to each well, that being based on the judgment that one well to each 640 acres would be economical and sound judgment. There are wells where you cannot get 640 acres around them. In that case, for example, where a well is drilled on an 80-acre tract I would let the well develop 80 acres. I would just take 80 acres as the amount developed in that case, that is all I would take.

Wells are spaced according to a wide variety of conditions. The outline of lease boundaries, the size of a lease and many other features are factors that determine the number of wells to be drilled on any given area. Under normal conditions a well producing from a sand formation will drain from 30 to 80 acres. Wells producing from porous limestone, as in the Amarillo field and the Hugoton field, will drain considerably more than that.

Some of the lease owned by the Company in Texas are outside of the sweet proven area and are in the sour gas area. I classified 10,680 acres in the Amarillo field as sour gas.

Sour gas is not suitable for domestic consumption.

I have valued the prospective acreage of the Company, Kansas, 597,919 acres, Oklahoma, 410,469 acres, Missouri, [fol. 565] 8,799 acres, and Texas, 13,940 acres, at One Dollar per acre.

In Carson County, Texas, in the Amarillo field the rock pressure of the wells has dropped in three and one-half years from 412 to 406 pounds, and during that time the wells have produced 69,996,000,000 cu. ft. of gas.

J. M. NESBIT, Chief Geologist and witness for the Company, testified:

The conferences for the sale of the 59,786 acreage of leases which were transferred to the Texoma, as of August 1, 1931, occurred in the year, 1930. Some of these leases which were afterwards transferred were acquired by the

Company in 1928. Along with the gas leases were transferred nine gas wells. The profit on the sale of these leases was in excess of One Million dollars, and on the sale of the gas wells was $11,000.00.

The number of gas leases held by the Company is approximately 7,000.

During the period from July 1, 1931, to November 1, 1931, the Company surrendered 61,471 acres of its gas leases as of not sufficient value to warrant the payment of rental.

Ross Stuntz, Superintendent of Production, witness for the company, testified:

The capacity of the pipe lines connected with the leases covered by purchase contracts is less than the amount of gas obtainable from the purchase contracts and said pipe lines are not sufficient to carry all of the gas available from these gas leases.

That in the year 1927 the Cities Service Gas Company produced only about 10% of the gas required for its system and purchased the balance; that at the present time (1931) in the month of June, the company produced 44% of its gas and purchased 56%; that the gas available under gas purchase contracts is not sufficient to take care of the peak demands of the company in winter; that the entire gas reserves of the company were bought for the sole purpose of assuring the gas supply and not for speculation and that, in his opinion all of such reserves are necessary for such [fol. 566] purposes.

The witness further testified that during winter peak demands it is necessary to turn in all wells connected to the system, whether owned by the company or under purchase contracts, and that under such conditions said wells, as a whole, on the average are capable of delivering only approximately 12% of their open flow; that during the winter of 1930 (the winter preceding the hearing) all the gas available to the system was necessary for service; that the Amarillo line was delivering 100,000,000 cubic feet a day, its full capacity, into the system and that without that line the system would have been 100,000,000 cubic feet per day short and that service would have failed; that there is

no gas purchased on the Amarillo line, all being gas owned and produced by the company.

[fol. 567] Mr. H. L. Eastman, Engineer and witness for the Company testified:

That the Amarillo line had at times been out of service, both from accident and for repairs, and the Company was able to maintain its service so that its customers knew nothing about it.

p. 245

On September 6, 1932, the Railroad Commission of Texas made the following order:

"Oil and Gas Docket No. 108

In re Conservation and Prevention of Waste of Crude Petroleum and Natural Gas in the Panhandle District

Austin, Texas, September 6, 1932.

Whereas, as public hearings at Pampa, Texas, on July 16, 1932, in Austin, Texas, on August 10, 1932, and in Amarillo, Texas, on September 1, 1932, after due notice, further testimony was heard with respect to waste of gas in the Panhandle Field; the control of the production and transportation of gas in such field; and with respect to the applications of Hagy, Harrington & Marsh, and others, to utilize the so called 'dry gas' produced from the West Panhandle Gas Field for the extraction of gasoline; and

Whereas, it appears that in the West Panhandle Gas Field, herein defined as the present producing sweet gas area and extensions thereof, in Moore, Potter, Hartley, Oldham, Hutchinson, Carson and that part of Gray County, Texas, embraced in Block 3, I. & G. N. Survey and Block B-2, H. & G. N. Survey, there exists an area comprising all that portion of the sweet gas area in Blocks 3, 4, and 7, I. & G. N. Surveys, and Block B-2, H. & G. N. Survey, Carson and Gray Counties, Texas, located east of a line drawn north and south through the southeast corner of Section 14, said Block 7, and the northeast corner of Section 116, said Block 4, in which there are some thirty-one (31) wells

which have been closed in for some time because there has been no market outlet for the gas, nevertheless in said area there are many wells which are producing gas inasmuch as the owners thereof have a market; and

Whereas, a Three Judge Federal Court, by opinion filed June 8, 1932, in what are generally known as the Common Purchaser Gas Cases, held that the statutes of Texas and orders of the Railroad Commission of Texas issued thereunder are void insofar as they undertake to compel gas pipe line companies to become common purchasers of gas under the provisions of the Common Purchaser Act; and

Whereas, beyond question the wells producing gas are draining gas from the properties upon which wells have been completed but have no market outlet, and will continue to so drain such properties, as well as others upon which no wells have been drilled and are not being drilled because no market exists for the gas; and

Whereas, the restriction of the use of such gas for light or fuel will result in confiscation of the gas of many lessees and its appropriation by those having a market outlet, unless, under Article 6008 of the Revised Statutes of Texas as amended, permits be granted for the use of such gas for other purposes than light or fuel; and

Whereas, The Attorney General, by opinion dated July 7, 1932, has ruled that, under certain circumstances, the granting of such permits would be conducive to the public welfare as contemplated by said Article 6008; and

[Fol. 5058] Whereas, Hugy, Harrington & Marsh and others have filed applications for the right to use gas produced from their wells in the area mentioned for the extraction of gasoline, and proof has been made that there is no reasonable prospect of finding a market for such gas,

for light or fuel, and consequently confiscation of their properties will take place if the use of gas be so restricted; and

Whereas, others similarly situated have informed the Railroad Commission of Texas that they will file similar applications for permits to extract gasoline from so-called 'dry gas'; and

Whereas, conditions with respect to drainage are particularly serious in the eastern portion of said West Panhandle Gas Field, as particularly described in the second paragraph hereof, and the owners of leases which have no market outlet are insisting that permits for extraction of gasoline be granted without delay unless ratable marketing of gas be obtained or some other means be adopted to prevent drainage of their properties; and

Whereas, those pipe line companies controlling the market outlet for gas refuse to purchase ratable and to take any gas except from their own wells, and, under said Federal Court decree, this Commission has been enjoined from enforcing the provisions of the Common Purchaser Act and must, therefore, if confiscation be prevented, either grant the application to extract gasoline from the gas, with the consequent loss of the residue and tremendous physical waste, or else prevent drainage and resulting appropriation by closing down all wells where drainage would be immediately affected, as in the area described in paragraph second above, and by requiring ratable production from other wells in the field;

Now, therefore, be it ordered that:

(1) All gas wells in the area last described in paragraph second above be closed in until such time as the owners of the wells in such area have a market which will insure ratable production, and outlet.

(2) Each well in the balance of the West Panhandle Gas Field being all of the field except the eastern portion as described in paragraph second above, from which gas is being used for light or fuel, shall be restricted to a flow of not more than 4% of its potential capacity, or so much of such potential capacity as may be necessary to take care of current demand for domestic and industrial uses.

(3) Wells in the West Panhandle Gas Field from which gas is being used for light or fuel in nearby towns are expected from subdivision one (1) of this order, on the ground of public necessity, pending further consideration of the facts to determine whether such wells can also be shut in.

Railroad Commission of Texas."

Later the Cities Service Gas Company, and others, brought suit to enjoin the enforcement of said order before a Three-Judge Court on the ground that the same was unconstitutional. Thereafter, the Railroad Commission rescinded said order, pending the determination of the constitutionality of said order.

Affidavit

The following affidavits were submitted by plaintiffs at the hearing before the 3-Judge Court:

[fol. 569] "H. R. STRAIGHT, of lawful age, being first duly sworn, upon oath, says: that he is now and for 17 years last past has been a resident of Bartlesville, Oklahoma; that he majored in Economics and graduated from Leland Standford University, a duly accredited college. That his occupation during said time has been carrying on the work of oil and gas business, including companies handling by-products of said substances and business similar to said business. That for the last ten or twelve years he has been the General Manager of Cities Service Gas Company and/or its predecessor companies. That in addition to his education along lines of the petroleum industry, affiant has had actual experience in the drilling of and supervising of drilling of oil and gas wells in Pennsylvania and other eastern fields for a period of about twenty years and approximately nineteen years in the Mid-Continent oil and gas area. That by virtue of his experiences and study of the Mid-Continent oil and gas region he had become familiar with the oil and gas fields in the states of Oklahoma, Kansas, Texas, New Mexico, Arkansas and Louisiana. That he is familiar with the experiences of the Kansas Natural Gas Company, The Wichita Gas Company, The Wichita Pipe Line Company and the Quapaw Gas Company from approximately the time such companies began to do business until their property was acquired by the Empire Natural Gas Company the predecessor of Cities Service Gas Company. That most of the difficulties of said companies arose or became acute largely because of frequent shortages of an adequate supply of gas or their difficulty in obtaining such supply.

Affiant further says that it is often impossible even with the aid of the most experienced and best qualified experts

to accurately forecast the existence, extent or durability of a gas field at any given place, and by reason of such fact any gas company that keeps abreast of usual competition must constantly keep a large reserve of gas acreage. That plaintiff and or its predecessor companies, during his knowledge of them, has always attempted to keep a sufficient gas reserve to insure dependable service to its patrons and has practically always been successful in so doing since the experiences of shortage of gas above alluded to occurred. That in said effort to constantly insure adequate gas reserves the plaintiff has at times had a far greater amount of acreage available to it than it now possesses and has uniformly found constant preserving of ample reserves [fol. 570] was advantageous. By reason of such policy, plaintiff has gradually built up a reputation for unexcelled service in the gas business.

Affiant says that for a long time past and now, the Cities Service Gas Company has acquired its gas reserves and acreage after exhaustive research; and as to the propriety and profitableness of the respective portions from time to time considered, and the acquisition of additional acreage from time to time, it is always a subject of serious consideration, conferences and exchange of ideas among its managing agents before such additional acreage is acquired. That in the judgment of affiant it is not only proper but reasonably necessary that plaintiff have for the business it conducts the gas acreage and reserves that it now possesses and such was the deliberate business judgment of the various managing agents who have collaborated with him in reaching the decisions from time to time to acquire such acreage.

Affiant further says that plaintiff does not now, nor has not for a number of years, owned any gas reserves or gas leases that are, or have been acquired for the purpose of sale, or are, or were held for speculation. That all the gas acreage that it now owns was acquired and is held by the plaintiff for the purpose of ensuring an adequate supply of gas to its patrons.

That plaintiff has but one single business, which is the business of supplying gas to its patrons through its network of pipe lines lying in the States of Texas, Oklahoma, Kansas, Nebraska and Missouri, which gas it wholesales to its customers; that it currently receives no income except

that produced from said business; that unless it uses a portion of the income from said business to maintain and preserve its leasehold estates, acreages and gas reserves, same will be lost to it and plaintiff will not be able to continue in the future to have a dependable gas supply that it customarily possesses nor give that dependable service which it has uniformly given to its patrons."

"George H. Band, of lawful age, being first duly sworn upon his oath says: That he is now and for the last sixteen years has been a resident of Bartlesville, Oklahoma; that by profession he is a mechanical engineer. That he is a graduate of the State Agricultural College, now known as Kansas State College, at Manhattan, Kansas, a duly accredited college, in which he majored in mechanical engineering and from which he duly graduated as a mechanical engineer in 1914. That thereafter he was employed by the [fol. 571] Westinghouse Electric Company at Pittsburgh, Pennsylvania, until he took employment with a predecessor in interest of the Cities Service Gas Company. That he has occupied positions in practically all branches of the field work pertaining to the production, transportation, sale and delivery of natural gas having successively been a field man, a meter man, superintendent of meters, conductor of industrial sales, and is now and for some time last past has been General Superintendent of operations over the whole system of Cities Service Gas Company located in the States of Texas, Oklahoma, Kansas, Nebraska and Missouri.

Affiant says that he is thoroughly familiar with all the pipelines, compressor stations and other equipment for transporting and delivering gas in said system. That in the usual course of his work it has become necessary for him to familiarize himself with the present fields of gas supply and to take part in all the conferences of executives and operatives in planning for the procuring of adequate gas reserves and the extensions of pipelines to the vicinity of such reserves not only for the dependable service of existing markets and utilization of the present sources of supply, but for the prevention of future shortages and the solving of problems that from time to time confront plaintiff in the expansion of its business and the consequent increase of reserves and equipment to accomplish and pro-

tpot such expansions. That he believes he is thoroughly familiar in a general way with all of the mechanical and operative problems that have in the past few years confronted plaintiff and which naturally will arise in the near future.

That plaintiff produces or buys, transports and sells at wholesale natural gas in quantities ranging from a minimum of about 100,000,000 cubic feet of gas a day to a maximum of about 330,000,000 cubic feet of gas a day. That a large portion of said gas is sold for domestic or heating purposes concerning which there is a high seasonal fluctuation and large daily and hourly variation. On account of this fact, among other things, it is necessary for plaintiff at all times to have large and dependable gas reserved and large pipeline capacity and a large number of compressor stations with separate units of power that may be thrown into or out of use upon short notice and to have more or less of a network of lines so that in case of breakage or washouts or other similar impediments the gas flowing in one portion of said system may be propelled to any other portion of the system desired.

[fol. 572] That about five years ago, plaintiff acquired a large gas reserve in the State of Texas and caused to be built to it a twenty inch pipeline, the maximum capacity of which is about 125,000,000 cubic feet of natural gas daily. That about the same time it caused to be built a sixteen inch pipeline for the purpose of conveying gas from what is known as the Seminole Field of Southern Oklahoma. That shortly thereafter it built a twenty inch pipeline from what is known as the Oklahoma City Field northward to the proximity of Wichita, Kansas. That shortly after the completion of said large trunk lines leading from its gas reserves it made eastern extensions to its existing gas pipeline system, one from the northern part extending a distance of approximately 110 miles from Ottawa, Kansas, to Sedalia, Missouri, and consisting of a twelve inch pipeline of the approximate ultimate capacity of 50,000,000 cubic feet of natural gas daily, together with an eight inch extension northward therefrom about 44 miles to the vicinity of Carrollton, Missouri; another extension being an eight inch line from Petrolia, Kansas, to the vicinity of Fort Scott, with facilities on eastward to the vicinity of Nevada, Missouri; the third extension being from a point a short

distance south of the City of Joplin, Missouri, eastward about 75 miles to the City of Springfield, Missouri, and consisting of a ten inch pipeline of the approximate ultimate capacity of 25,000,000 cubic feet of natural gas daily.

That it is and has been for many years last past the custom of plaintiff to frequently hold conferences not only upon present problems, but to estimate and figure out the probable future contingencies and problems that will arise in the usual course of its business. That in the remote past plaintiff has had unfortunate and costly experiences because of lack of adequate gas supplies and reserves for pipeline capacity, arising partly because of premature and unexpected exhaustion and depletion of gas reserves partly on account of breakage of lines with inadequate auxiliary equipment to serve during the respective emergencies. On account of this experience this affiant and the executives of plaintiff have become familiar with the perplexing and costly problems that arise because of not having reserve line capacity and gas supply, and in the recent years last past have sought to so amplify their line capacity and gas supply and reserves that it may at all times furnish a dependable gas supply to the customers who serve the greater [fol. 573] part of the State of Kansas and a large part of the State of Missouri. To obtain a satisfactory degree of dependability it has been necessary for plaintiff for many years past, and is now necessary for it, to have large natural gas reserves located in as diverse directions from the center of its system as is practical and with the view of preserving a dependable supply at the lowest cost it acquired large supplies or reserves in the Seminole Field, the Oklahoma City Field, the Texas Panhandle Field, the Oklahoma Panhandle Field, the Hugoton Field, other Western Kansas Fields, and Northeastern Oklahoma. That the acquisition of these respective supplies and reserves has been a matter of serious consideration by the meeting of managers of plaintiff for the past several years and no supplies or reserves are ever acquired except after a deliberate decision by its managing agents that they are necessary for the dependable operation of the only business conducted by the plaintiff, which is that of gas producing, transporting, selling and delivering which is carried on through its integrated pipeline system in the aforesaid states. That plaintiff has no other business than the said

business and has acquired no gas acreage for any other purpose than for the serving of said business, and does not now and has not in the recent past acquired any gas acreage for speculative purposes or to sell to others.

That plaintiff at all times employs and uses in its customary and ordinary course of business a large staff of expert and experienced geologists who continuously by use of maps and all the other paraphernalia known to petroleum geologists attempt to analyze and delimit the known developed fields and also to discover and demonstrate the productivity of other areas not now developed or used for gas production. That notwithstanding the large experience of affiant and the managers of plaintiff and the assistance of the geological staff mentioned it is not always possible for plaintiff to foretell the extent or productivity of areas examined and analyzed or of new fields. That if plaintiff should wait for the discovery and development of new fields by others it would probably frequently experience shortages of supplies necessary for its markets while so waiting for others to take the lead, and also if plaintiff should abjure all initiative on its part and wait for others to develop gas fields it would be compelled to pay exorbitant prices for its gas reserves and supplies and at times be confronted with the alternative of either paying pro-
[fol. 574] hibitive prices or being short of gas. That in acquiring new acreage plaintiff gives great consideration to the proximity of same to its present or projected lines and practically all of plaintiff's gas acreage, amounting to about one and one quarter million acres, is located within practical striking distance of present or prospective lines.

That plaintiff ordinarily considers the building of large trunk lines over periods varying from one to five or more years in advance of the time they are built. That the Seminole line was a piecemeal construction, section of same being build progressively as fields from which it served were discovered, the last section of which was considered about two years before same was built. The Oklahoma City line was under consideration for approximately two years before it was built. The Texas Panhandle line was under consideration about five years before it was built. Plaintiff is now and for about two years last past has been considering the building of a line from the Hugoton Field of Kansas and Oklahoma to join with its system in the

vicinity of Wichita, Kansas, and to run through the large acreage of plaintiff intervening between the termini of said line.

That on account of the eastern extension aforesaid into Northwestern, Western and Southwestern Missouri, plaintiff has very little surplus line capacity during normal times and considering normal peaks. If the markets along the Sedalia, Nevada and Springfield lines develop in the proportion that new fields or markets normally develop, plaintiff's line capacity and compressor station capacity will shortly become inadequate. That because of said extensions being so new affiant believes that the markets along same will radically increase and that much more gas will be necessary to be carried through said lines. That recently the Railroad Commission of Texas issued and served upon plaintiff an order requiring it to shut down twenty three of its gas wells in the Panhandle of Texas and limiting the production of the remainder of its gas wells in the Texas Panhandle to four per cent of their respective open flows. That the said gas wells have an average open flow of approximately 20,000,000 cubic feet daily. That if said order be continued in operation it will prevent plaintiff from taking more than 32,000,000 cubic feet of gas daily from the Texas Panhandle, whereas the capacity of its said Texas Panhandle line is approximately 125,000,000 cubic feet and it is accustomed at peak times to use it to near its capacity. By reason of said order and while it continues [fol. 575] in force plaintiff will be compelled to procure from 50,000,000 to 100,000,000 cubic feet of gas from other sources and through other channels than those now in use, and plaintiff will be compelled to develop and use gas reserves not now developed and in all probability will be compelled to resort to its holdings in the Hugoton Field in Kansas and Oklahoma. That on account of the Missouri extensions mentioned it has already enlarged constrictions in its Southern Kansas trunk line and Quapaw line from twelve inches to sixteen inches thereby giving to plaintiff more line capacity to said Missouri markets. That on account of said extensions into Missouri and the said consequent enlargements plaintiff has been, and is holding the Hogshooter compressor station in constant readiness to serve its said pipeline systems and especially its said extensions into Missouri. That by use of said compressor

station it would add a transmission capacity of approximately 20,000,000 cubic feet of natural gas daily and by such use it can accomplish such result much cheaper than in any other manner. That while said order of the said Texas Railroad Commission is operative it will be necessary for plaintiff in cold weather to use said Hogshooter compressor station to increase the transmission capacity of its lines from whatsoever source it gets its added gas supplies, and whether said Texas order remains in force or not upon resumption of normal financial conditions or the natural growth of the Missouri markets along the said newly constructed extensions the economical operation of plaintiff's system will require the operation of the Hogshooter compressor station. That when the said Hugoton line is built this will add greatly to the supply of gas that can be delivered at Wichita; but to transmit said gas to our eastern extension lines or other markets east of Wichita it will be necessary to add additional expensive compressor units and probably to build additional transmission line capacity. However, by the use of Hogshooter station and the use of the Southwestern portion of plaintiff's pipeline capacity it can increase the volume of gas for delivery to said eastern extensions and the markets north of Ottawa by approximately 20,000,000 cubic feet daily. That until it becomes imperative to build the Hugoton line to add gas supplies for plaintiff's markets, as aforesaid, it would be much more economical to strengthen the transmission power of the southeastern portion of plaintiff's pipeline system and use the Hogshooter compressor station, and this is the course that it is the present intention of plaintiff to pursue. [fol. 576] That the said strengthening of the transmission power of the southeastern portion of said system will not permanently solve the question confronting plaintiff as to the increase of the transmission power of its entire system, but the use of the Hugoton Field in Kansas and Oklahoma is bound to become necessary in the not far distant future in the ordinary course of the business of said plaintiff."

"H. L. Montgomery, of lawful age, being first duly sworn upon oath, says that he is now and for thirteen years last past has been a resident of Bartlesville, Oklahoma, and during the last ten years of said time has been the Manager of Cities Service Gas Company and its predecessor com-

ponent companies; that he is now and for several years past also been Vice President of Cities Service Gas Company. That in the performance of his duties as such Manager he has become familiar with the prices charged for natural gas by our pipe line companies in Kansas and other adjoining states, and is familiar with the prices charged by plaintiff in all States in which it operates and is in a general way familiar with the distributing companies that purchase gas in said States and their respective corporate affiliation.

Affiant further says, that plaintiff is now and has been for many years last past selling Domestic gas in Kansas at the respective City Gates of the distributing companies which purchase from it at approximately the rate of forty (40) cents per thousand cubic feet, except that it is and has been thus selling to distributing companies located in the proximity of what is known as the "Southern Kansas Trunk Lines" at the approximate rate of thirty eight (38) cents per thousand cubic feet. That plaintiff does not now and never has made any differentiation whatever as to price between sales made to distributing companies that were affiliated with it and sales made to unrelated distributing companies on account of the existence or lack of corporate relationship. That where conditions are essentially similar it is now and has been in the past selling gas to affiliated companies at the same rate at which it sells to unrelated companies. That a tabulation truly showing its sales to unrelated distributing companies in the State of Kansas giving rate per thousand cubic feet, number of customers and approximate population in the different towns is hereto attached marked Exhibit "A" and made a part thereof. That a tabulation truly showing its sales to unrelated distri- [fol. 577] bution companies in the State of Missouri, giving rate, per thousand cubic feet, number of customers and approximate population of the respective towns, is hereto attached and marked Exhibit "B", and made a part hereof. That a tabulation truly showing contract for sales to companies that were unrelated to plaintiff at the time the contracts were made, but are now owned by companies affiliated with plaintiff, giving rate per thousand cubic feet, number of customers and approximate population of respective towns, is hereto attached marked Exhibit "C" and made a part hereof. That several of the unrelated companies to

which plaintiff sells gas are adjacent to or within striking distance of other large gas pipe lines and practically all of the unrelated companies to which plaintiff sells are either near said large pipelines or smaller pipe lines, which more clearly appears from a map showing pipeline system of plaintiff and that of other large pipelines near said unrelated markets which is marked Exhibit "D" and made a part hereof.

That the City Gate rate of forty (40) cents was fixed by the Public Utilities Commission of the State of Kansas, the predecessor of the said Public Service Commission, in 1923 and was decreed by said Commission at said time, composed of C. M. Reed, H. A. Russell and J. W. Greenleaf as Commissioners, to be the reasonable City Gate rate for main line gas except as to said Southern Kansas Trunk Line for which it was decreed by said Commission the thirty eight (38) cent City Gate rate was the reasonable price. That so far as Affiant is informed no application to said Public Utilities Commission, or Public Service Commission of Kansas, has been made by citizens in the towns affected for the lowering of the Gate rate prices so fixed as aforesaid.

That affiant is familiar with the establishment and growth of the component companies that entered into the formation of Empire Natural Gas Company now known as Cities Service Gas Company. That said component lines were built piece meal from time to time to reach markets progressively acquired and in the fields of supply necessary to be reached.

That at the respective times during which those pipelines were thus intermittently contracted, the distributing companies now receiving gas from Cities Service Gas Com- [fol. 578] pany were not owned by Cities Service Gas Company, and for the most part at the time the contracts for the sale of gas at the City Gates were made were not owned by or affiliated with any of the pipeline companies which were brought together to compose plaintiff's present intergrated system of pipelines.

Affiant says that the domestic rate charged by plaintiff in Kansas is in line with, or lower than the rates charged by comparable pipe line systems under similar circumstances. That the usual Gate rate price of Panhandle and Eastern corporations where taken from the Texas Panhandle and Hugoton field is through Kansas into Missouri is in said

States approximately forty (40) cents per thousand cubic feet. That the usual City Gate price of the Community Natural Gas Company, a subsidiary of the Lone Star Gas Company, so far as it pertains to sales in Oklahoma, is approximately forty five (45) cents per thousand cubic feet. That the schedule of rates of the Natural Gas Company of America which takes gas from the Panhandle of Texas through the intervening States to a point near Joliet, Illinois, their sales, some wholesale, if applied to the load factors existing in the markets of plaintiff in Kansas, would be considerably higher than those charged by the plaintiff in Kansas. That about ten days ago the Public Utilities Commission of Ohio fixed as the reasonable City Gate rate for the Ohio Fuel Gas Company to charge to the distributing companies of Columbus, Ohio, rate of thirty nine (39) cents per thousand cubic feet. And affiant further says, that the distance from the place of production of the gas to the city of Columbus is very much less than the distance from plaintiff's greatest source of supply to its largest markets.

Affiant further says that on account of the experiences of its predecessor component companies in the past as to gas shortages, the necessity of maintaining at all times an ample and dependable gas reserve has been strongly impressed upon affiant and the officers and directors of Cities Service Gas Company, and they have without raising the aforesaid Gate rate, acquired large and dependable gas reserves, acquisition of which was the result of the deliberate judgment of the directors and officers of plaintiff, including this affiant; that it was necessary to have and continuously maintain the present gas reserves or gas reserves of similar extent and dependability.

That it is very desirable to have gas reserves located in [fol. 579] as diverse a direction from the geographical center of plaintiff's system and markets as possible, and plaintiff's gas reserves have been acquired largely with relation to its markets and its existing or projected pipe lines and the respective capacities of such pipe lines. That within the last five or six years plaintiff has made enormous investments in additional pipe line and transportation facilities in order to utilize its gas reserves and ensure a stable and dependable supply to its customers and to keep pace with the growth of its markets, not only in its new extensions into the State of Missouri, but also into the State of Kansas,

and during such period it has not raised, nor sought to raise the City gate rate fixed as aforesaid by said Commission."

Exhibit "A"

Foreign Distribution Properties Served by Cities Service Gas Company, Kansas

Community	Company	(1930 census) population	1-1-32 customers	Town border rate domestic
Altamont	American Gas Co.	598	215	38¢ M. c. f.
Anthony	Western Natural Gas Co.	2,497	466	40¢ "
Atchison	Kansas Power & Light Co.	13,034	2,500	40¢ "
Bassett	Allen County Supply Co.	104	60	30¢ "
Baxter Springs	Baxter Springs Gas Co.	4,541	993	38¢ "
Cherokee	American Gas Co.	1,158	147	38¢ "
Clearwater	United Gas Service Co.	981	133	40¢ "
Columbus	American Gas Co.	3,235	704	38¢ "
Conway Springs	United Gas Service Co.	981	183	40¢ "
Emporia	Kansas Electric Power	14,007	2,743	40¢ "
Galena	American Gas Co.	4,730	623	38¢ "
Harper	United Gas Service Co.	1,485	245	40¢ "
Lawrence	Kansas Public Service	13,726	4,241	40¢ "
Leavenworth	Kansas Electric Power Co.	17,466	3,357	40¢ "
Lebo	Ross Gault	500	70	40¢ "
Lyndon	United Gas Service Co.	742	69	40¢ "
Melvern	United Gas Service Co.	445	55	40¢ "
Oswego	American Gas Co.	1,845	407	38¢ "
Quenemo	United Gas Service Co.	564	94	40¢ "
Scammon	American Gas Co.	1,093	131	38¢ "
Thayer*	United Gas Service Co.	495	140	30¢ "
Treece	Baxter Springs Gas Co.	740	47	38¢ "
Wellington*	Wellington Gas Co.	7,405	2,012	10¢ "
Totals		92,755	19,406	

* Local Gas.

Exhibit "B"

Foreign Distribution Properties Served by Cities Service Gas Company, Missouri

Community	Company	(1930 census) population	(1-1-32) customers	Town border rate domestic
Carl Junction	Carl Junction Gas Co.	1,500	200	40¢ M. c. f.
Holden	Interstate Gas Co.	1,807	127	40¢ "
Kingsville	Interstate Gas Co.	237	21	40¢ "
Lexington	Missouri Gas & Electric Service Co.	4,595	643	40¢ "
Marshall	Missouri Gas & Electric Service Co.	8,103	881	40¢ "
Oronogo	Citizens Gas Co.	575	115	40¢ "
Platte City	Missouri Gas & Electric Service Co.	587	54	40¢ "
Pleasant Hill	Interstate Gas Co.	2,330	243	40¢ "
Smithfield	Carl Junction Gas Co.	150	20	40¢ "
Weston	Missouri Gas & Electric Service Co.	1,028	90	40¢ "
Totals		20,912	2,405	

Exhibit "C"

Properties in Missouri Served by Cities Service Gas Company, Formerly Owned by Urban Service Company and Now the Property, Ozark Distributing Co. (Subs. of Gas Service Co.)

Community	(1930 census) population	(1-1-32) customers	Town border rate domestic
Carrollton	4,058	163	40¢ M c f
Concordia	1,140	43	40¢ "
Norborne	1,190	21	40¢ "
Sweet Springs	1,641	76	40¢ "
Totals	8,029	303	

Other towns included in contract between Urban Service Company and Cities Service Gas Company, but to which pipelines were never built are:

Fulton, Higginsville,
Glasgow, Hardin,
Fayette, Norborne
Slater,

all in Missouri.

The Springfield Gas & Electric Company serving Springfield, Missouri (Population 1930 Census 57,527, No. of customers 1-1-32, 7201) was a foreign distribution property when the contract was signed July 26, 1929, but has since become an affiliated company. The town border rate on domestic gas is 40¢ M c f.

Depreciation of Overheads

The following was submitted to the District Court on depreciation of overheads:

"The following tabulation shows the amounts of overheads included in the valuations of Black and Hamilton, respectively, and the last column the allowances which were made by the Commission:

[fol. 581]

Undistributed Overheads Depreciated

Item	Black		Hamilton		Commission	
	RCN	PV	RCN	PV	RCN	PV
Administration & Legal Expense	$1,287,348	$1,144,475	$348,586	$348,586	$340,094	$304,084
Taxes During Construction	875,171	778,044	769,174	769,174	875,171	778,044
Interest During Construction	4,323,212	3,859,204	6,337,986	6,337,986	4,351,934	3,883,282
Miscellaneous Construction Expense			769,174	769,174	680,187	606,169
Engineering & Supervision	3,196,878	2,846,163	3,459,011	3,166,329	3,218,585	2,881,900
Total	9,682,609	8,627,889	11,719,931	11,427,249	9,465,971	8,454,579
Reduction in Rate Base by Depreciation of Overheads other than Eng. & Supt.		704,905				673,807
Replacement Reserve Allowance @ 2.96%		280,605		346,910		280,193

[fol. 582] "These overheads were not depreciated by Hamilton with the exception of the item for engineering and supervision. The allowance for annual depreciation testified to by Eastman amounted to $3,276,325.07. Eastman unintentionally failed to make an allowance for depreciation on the item of Engineering and Superintendence. Engineering and Superintendence was included by Hamilton in the amount of $3,459,011.00 and the proper allowance for depreciation if the Hamilton valuation is adopted would be 2.96% of that amount or $102,387.00.

Eastman's Exhibit No. 27	$3,276,325.07
Correction for Engineering & Superintendence	102,387.00
	$3,378,712.07

The allowance by the Commission for annual depreciation and depletion was $1,786,338.88. The Commission, as shown above, did deduct accrued depreciation from all of these overheads in arriving at the total value found. The Commission did not make any allowance in their annual depreciation computation for these items.

"If it is not proper to depreciate the overheads as shown in the above tabulation there should be added to the Commission's value the sum of $673,807.00 and if it is proper to depreciate them there should be added to replacement reserves on the basis of Black's value the sum of $286,605.00 and on the basis of Hamilton's value the sum of $346,910.00 and on the basis of the Commission's finding the sum of $280,193.00.

Annual Depreciation and Depletion Requirements

The following agreed statement was submitted to the District Court on annual depreciation and depletion requirements:

"Under this heading in its opinion, beginning at page 110, the Commission discusses requirements for physical equipment other than gas leases, requirements pertaining to gas leases, general development expense capitalized, [fol. 583] amortization of non-producing leases, dry hole expense and annual requirements for depletion of producing leases. All of these matters will be considered under this heading.

"The only evidence in regard to replacement reserves covering all of these items was that of H. L. Eastman in support of his Exhibit 27 in which he set up reserves totaling $3,276,325.07 divided among the several accounts as appears by the exhibit, which is as follows:

Production Field Measuring Stations	$41,635
Production Other Structures & Equipment	3,401
Production Gas Well Construction & Equipment	183,882
Production Field Line Equipment	322,492
Production Drilling & Cleaning Equipment	3,283
Transmission Rights of Way	91,183
Transmission Other Structures	4,884
Transmission Measuring Stations	45,491
Transmission Compressing Station Structures	76,682
Transmission Compressing Station Equipment	283,625
Transmission Line Equipment	1,103,071
Transmission Other Equipment	416
General Other Structures	3,657
General Office Equipment	10,782
General Store Equipment	169
General Shop Equipment	1,350
General Stable Equipment	54
General Laboratory Equipment	837
General Tools & Implements	5,136
General Other Equipment	1,525
Sub-total	$2,183,555
General Development Expense Capitalized	532,530.77
Amortization of non-Production Leases	314,981.68
Dry Hole Expense	174,747.74
Depletion of Producing Leases	70,509.88
Total	$3,276,325.07

In Exhibit 27 Eastman unintentionally omitted an annual allowance for the depreciation on engineering and superintendence. The Commission used an average of 2.96% for annual depreciation on all physical property, which is accepted by the parties. Applying this 2.96% to the

account of engineering and superintendence resulted in a figure of $102,387.00 which should be added to Mr. Eastman's total for replacement reserves of $3,276,325.07, making the total $3,378,712.07.

"The average of Eastman's allowance for replacement reserves, when applied to Hamilton's valuation of those accounts, results in an average per cent of 3.01, as appears in the opinion, page 111. The witness P. McDonald Biddison, testify for respondents, testified:

[fol. 584] 'I would say in general that a minimum rate of depreciation for any natural gas pipe line system would be 4%, and that in many cases it would have, if your fields are short lived, to be on up well above 4%.'

"The Commission calculated in per cents the replacement reserves testified to by Eastman as to the several accounts as applied to the value of the property found by Hamilton for the accounts respectively and arrived at the several per cents set out in the table on pages 110 and 111 of the opinion. The application of these per cents to the several values found by the Commission resulted in an average per cent of 2.96 for all depreciation and amortization purposes, exclusive of leases.

"The Commission undertook to average replacement reserves requirements and found such requirements for the property in existence on September 1, 1931, to be $1,889,022.00; for the property in existence December 31, 1930, to be $1,693,312.00 and for the property in existence June 30, 1931, to be $1,712,216. The Commission then averaged the last two figures notwithstanding the fact that the two annual periods used by it were only six months apart and overlapped and arrived at an average figure of $1,702,764.00, which is the allowance made by the Commission for annual depreciation on physical property other than leases."

[fol. 585] "Amortization of non-Producing Leases"

Under this heading the Company seeks to include in its annual reserve allowance $314,981.68 for the amortization of non-producing leases, which is claimed as necessary to amortize the cost of leases owned by the Company which are

not producing. This figure of $314,981.68 is taken from the books and covers the experience of the Company for the year 1930 and includes amortization for the year 1930 on the non-producing leases sold to the Texhoma Company in the latter part of 1931.

General Development Expense

The company asks for an annual reserve allowance of $532,530 for general development expense capitalized.

Eastman testified that this item includes the following character of expenditures; Cost of acquiring leases; geological expense; lease rentals.

The cost of acquiring leases was made up of salaries and expenses of men engaged in acquiring leases and scouting expenses.

The item of $532,530 represents the expenditures for leasehold development charged to capital investment during 1930. This sum is also found on the last page of Eastman's Exhibit 8, which shows the "Net Additions to Plant and Investment" each year from 1923 to 1930, inclusive, and for the first six months of 1931, under the column headed "1930," and it was added to the plant investment account in the books in that year. It includes expenditures for development of leaseholds, consisting of cost of acquiring leases, geological costs, and lease rentals during that year incurred in part in connection with leaseholds and wells sold to the Texhoma Company during the latter part of 1931, and subsequently the Texhoma repaid this expense to the Cities Service Company. The above amount is estimated as the future annual expenses for leases for those purposes. These general development expenss are capitalized. Rentals on non-producing leases amounted to $329,917.00.

[fol. 586] "Dry Hole Expense"

The appellees asked for an annual allowance in the amount of $174,474.74 for dry hole expense. This is an amount which the Company seeks to have allowed as an annual allowance for expenses in drilling dry holes. This figure is based on the experience of the Company for the year 1930. In 1930, the Company drilled ten dry holes on scattered acreage in Oklahoma, Kansas and one well in

Texas, none of which was drilled upon the territory now designated as proven.

"The Commission adopted Hamilton's figure of $70,509.88 for depletion of producing leases. If this Commission's theory that non-producing leases should not be amortized is adopted, respondents contend that if all leases are found to be used or useful the allowance for depletion of producing leases of $70,509.88 should be increased in the sum of $314,981.68 to cover that portion of the cost of leases that has hitherto been amortized through the allowance of depreciation on non-productive leases and that if the Commission's theory that overheads should be depreciated is adopted there should be added to the Commission's allowance for replacement reserves the sum of $280,193.00 and to Hamilton's allowance the sum of $244,523.00, each figure being 2.96 per cent of the overheads included in the values respectively which have been depreciated by the Commission.

"In this connection Mr. Eastman testified as follows:

'Q. What is the last item we have here, depletion of producing leases?

'A. Depletion of producing leases is—represents that portion of the leases which have been depleted during the past year on account of the gas taken from that lease. * * *

* * * * * * *

'Q. Now how did you arrive at your figure of $70,509.88?

'A. I didn't arrive at that figure myself, it was calculated by our operating departments. * * * A. I didn't arrive at it. Those calculations are currently made by the operating department, based on geological information, and operating records. * * *"

[fol. 587] Net Income

It was agreed by the parties before the District Court that the net income of the Cities Service Gas Company, before depreciation and depletion and before adjustments for Henry L. Doherty & Company payments for the year ended December 31, 1930, was $8,829,480.71; for the year ended June 31, 1931, $8,741,809.14 and for the year ended June 30, 1932, $7,861,516.85.

Included in the expense for the year ended December 31, 1930, was an item of $75,022.33, representing payments

made to Henry L. Doherty & Company, which the Commission disallowed as an operating expense and added to the net income of the company for the year ended December 31, 1930.

Included in the expense for the year ended June 30, 1931, was an item of $68,882.05, representing payments made to Henry L. Doherty & Company, which the Commission disallowed as an operating expense and added it to the net income of the company for the year ended June 30, 1931.

Included in the expense for the year ended June 30, 1932, was an item of $52,297.13 representing payments made to Henry L. Doherty & Company, which the Commission disallowed and added to the net income of the company for the year ended June 30, 1932.

Included in the operating expense for the year ended June 30, 1932, was an item of $50,000.00 for the amortization of expense for the present investigation, which the Commission disallowed and added it to the net income for the year June 30, 1932.

"For the reasons stated in the opinion, the Commission also added to net income for each of the years ended December 31, 1930, and June 30, 1931, $78,874.00 because of the fact that no other figure appeared in the record. This addition is in error as the net income used by the Commission for the year ending December 31, 1930, in amount $8,829,480.71, included a construction credit for that period amounting to $118,488.75 and the net income used by the Commission for the year ending June 30, 1931, in amount $8,741,809.14, included construction credit for that period amounting to $114,118.00."

[fol. 588] Average Value During Period Covered by Earning Statement

The following agreed statement was the evidence submitted to the District Court on the average value during period covered by earning statement:

"Under this heading the Commission's opinion, pages 121 to 124, purports to set out values of the property as of September 1, 1931, July 1, 1931, January 1, 1931 and July 1, 1930, and from such values to determine an average value.

"The net additions to fixed capital tabulated on page 123 of the opinion were taken from the fixed capital account of

the Cities Service Gas Company by the Commission's auditor. Eastman testified that under the accounting practice of the company there was a lag between the time a line was completed and placed in operation and the time the job order was closed and posted to the fixed capital account of from one to three years and that therefore the fixed capital account did not reflect the total property of the company on the several dates used by the Commission.

[fol. 589] Eastman testified on cross-examination as follows:

"Q. Exhibit No. 88, which you referred to yesterday, was prepared from the books of your company as to unfinished construction?

"A. Yes, sir.

"Q. Now, as I understand from your explanation yesterday, the books did not reflect the actual situation as to unfinished construction?

"A. They reflect the actual situation as to uncompleted job orders, they do not as to the dates on which entry is made, the books reflect the actual time as to the construction of the property.

"Q. That is, you cannot refer to your books and find out whether construction is finished?

"A. Construction is finished, as I tried to explain——

"Q. I understand that it is done before it appears on the books, simply answer the question. I want to know if I am right on this, you cannot refer to your books and determine whether or not construction is completed and in use?

"A. Yes, sir, you can refer to the books——

"Q. What books?

"A. The same items you have here, because the construction is done before these entries are ever made.

"Q. Is the construction completed before the money is expended?

"A. The construction is completed at the same time the money is expended. The money is expended before it appears on the books.

"Q. Well, now, when a construction job is started and money is expended for labor or material, what entry is made upon the books of the company?

"A. That entry is made on the books at that time.

"Q. Where is that entry made, in what account?

"A. Well, it depends entirely on the nature of the construction as to what account it would be. The usual procedure on construction of any project, is for the construc[fol. 590] tion to be approved by means of what we term a requisition. The requisition is approved, authority given for proceeding with the construction work, a job order is opened, thereafter charges in connection with the construction are made to this job order.

"Q. That did I understand you to say the construction was completed before the entires were made on the books?

"A. In some cases, yes, in small jobs.

"Q. Well, on your large jobs, do you go ahead with construction and then expend the money?

"A. Yes.

"Q. That payment is then placed upon the books, isn't it?

"A. As the money is actually spent, yes, sir.

"Q. Then none of your larger construction would the construction be completed before the money was expended and placed upon the books?

"A. It might be, I did not say it would be.

"Q. That is some of your larger lines, you think the construction might be completed before the money was expended?

"A. No.

"Q. Well, before the money is expended

"A. Construction in that case will be completed before the final entries go on the books.

"Q. But the larger part of the entries should be there?

"A. I presume so, yes, on a large job.

"Q. Well, then it is impossible for us to determine from the examination of your books what construction was completed during the last 18 months?

"A. I believe that is generally correct, as I testified yesterday.

"Q. And it is impossible for us to determine from an examination of your books, what construction was incomplete on September 1st, and in operation?

"A. That is generally correct, yes, sir.

"Q. Well, then, Mr. Eastman——

"A. Probably true because of the law between the time the work is actually done and the entries being made on the books, because there is bound to be a certain lag in there, however, it is perfectly possible to tell by inspection of the property at any certain date what work is done.

[fol. 591] "Q. Take the Wichita compressor station, what would be the lag there?

"A. The lag in this case has been in the neighborhood of a year.

"Q. That is, the property was in operation a year before the entries were made?

"A. The exhibit which you have here lists uncompleted job orders as of June 30, 1931. The property actually went in operation in the fall of 1930.

"Q. Can you give us the dates on which these entries were made on the books?

"A. That varies almost from the time the work actually started, up until June 30, 1931, and possibly some since.

"Q. The items of expenditures were made, and were entered on the books?

"A. Yes.

"Q. There was no particular gap there, especially, of a year between the time the expenses were made and entered on the books, was there?

"A. There might be in case of disputed charges.

"Q. These would be very few, would they not?

"A. I think so.

"Q. In other words, Mr. Eastman, they take your book value then does not correctly reflect the value of the property in operation?

"A. No, sir, the book value does not reflect the value of the property in operation. We have made no such claim. I believe that was the purpose of Mr. Black making his appraisal, to determine the value of the property.

"Q. I mean, it does not reflect the actual cost?

"A. No, sir, there is always a lag.

"Q. Will you furnish to the commission the unfinished construction at the date September 1st, 1931; and also the construction which was finished and put in operation for an 18-months' period preceding that date?

[fol. 592] "Mr. Garver: I don't think we ought to go to that trouble and expense. Mr. Eastman knows personally these units are in operation.

"Mr. Hatcher: Your books don't reflect it and it is hard for us to get it.

"Mr. Garver: You are not accepting our books for that purpose. You won't take the book value of our plant ac-

count for this rate base, these items are all completed, Mr. Eastman has testified they are in his valuation and they are in Mr. Black's valuation, Mr. Black knows whether they are or not.

"Mr. Hatcher: I believe Mr. Eastman; he could not go through and give us the exact dates, there is no way the commission can know when this property was put in operation.

"Mr. Garver: You can analyze those job orders, why should we put in weeks doing it.

"Mr. Hatcher: We cannot analyze the job orders.

"Mr. Garver: A job covers $5,000,000, a contractor is paid a monthly statement of cost on the job order and when the payment is completed

"Mr. Hatcher: That does not tell us when the property went into operation.

"Mr. Garver: It is all in this valuation.

"The Witness: I think Mr. Black can identify practically every bit of that property, being in his valuation.

"Mr. Hatcher: Was not used and useful, covered by the period covered by his valuation?

"A. It certainly was. I testified it was in operation.

"Q. Will you furnish us that information?

"A. No, sir; I won't.

"Q. Will you furnish it, Judge Garver?

[fol. 343] "Mr. Garver: No, I don't think we should be asked to go to that expense. If anybody wants to go to the trouble of analyzing out these job orders, it would be easier to take this list of Mr. Montgomery's and see if they are in operation.

"Mr. Hatcher: We have analyzed the job orders. He testified that they do not reflect the actual condition.

"Mr. Garver: You have not made any effort to determine whether those units are in operation or not. If you are in doubt about it, go look at them and see.

"Mr. Stone: Mr. Black's inventory ought to show that, comparison would show it.

"Mr. Garver: Most of this stuff is units of compressor stations. He went to those stations and checked our inventory and used it.

"Mr. Hatcher: It would not show when it went in operation.

"Mr. Garver: It doesn't make any difference when it went in operation, if they were in operation September 1st.

"Commissioner Hill: Is it not a question of whether or not this property is used or useful upon the date September 1, 1931?

"Mr. Garver: That is it. Mr. Eastman's testimony is based his dates put in operation, if anybody doubts, let them go look at the property and not at the books.

"Commissioner Hill: We have a valuation upon the property as of that date, there seems to be some little question, but it does not seem to me it is material.

"Mr. Garver: There is no question between Mr. Black and Mr. Eastman, and because Mr. Black sent his men to the property and checked the property, we gave them the information they requested and if his men want to take the inventory and determine depreciation and to do that, they had to know the things were in operation and to determine the fact as to whether they were in operation or not, they could find out at the plant itself.

[fol. 594] "Mr. Hatcher: If ten or fifteen million dollars worth of this property was put in operation on September 1st, it was not there for the purpose of earning a return during the period covered by this investigation, and we would like to know what that property amounts to, if it was not there and available for earning during that period, it would distort our picture when we get to arriving at the property.

"Mr. Stone: Have you compared it with Mr. Black's inventory to see whether it is not included in the inventory?

"Mr. Hatcher: It is perhaps included. We want to know whether it was in operation. He cannot give us the date it went into operation.

"Mr. Stone: It don't make any difference, if it was in operation September 1st, at the time of the valuation.

"Mr. Hatcher: You cannot compare the value of September 1st, with earnings for September 30th.

"The Witness: The first item amounts to $237,000, approximately. B-12888 covers erection of two 1000 H. P. units, Moreland Compressor station. These were constructed and went into operation in the fall of 1930.

"Q. What month?

"A. I cannot tell you the exact month, I presume October or November. I know that they went into operation there

the winter of 1930. That covers both units, a total of $257,000. The next item amounts to $366,000, job order B-13889, three compressor units at Wichita. Those were installed some time about the same time as the Moreland units, in the fall of 1930, have been in operation ever since. The next item is $32,000, construct gas pipe line, Lyons, Kansas, to Nelson, Nebr. That line was constructed in the early part of 1930 and in 1931 and was in operation.

"Q. Do you know the month when the gas was first turned into that line?

"A. No, Mr. Black has in his possession some large maps which show the dates of construction of each one of these lines.

into Springfield, Mo., recently?

[fol. 395] "Q. Was there an extension of the line going

"A. No.

"Q. When was the last extension made on that line?

"A. Going into Springfield?

"Q. Into Missouri, the Sedalia line?

"A. There was an extension to that line.

"Q. When was the extension made to that line?

"A. Most of that, during the latter part of 1930 and the first part of 1931.

"Q. You don't know the time when the gas was put in that?

"A. There were several extensions made to the Sedalia line.

"Mr. Garver: Any items of lines in that Exhibit 88, the date of construction appears on Mr. Black's valuation, does it not?

"A. Yes, the next item of any importance is $151,000, purchase leases and wells in the Craig field, B-12845. Those leases and wells were purchased, approximately two years ago.

"Q. When was the gas turned into the field for storage purposes?

"A. A year ago this past fall. That would be in the fall of 1930.

"Mr. Stone: Do you mean a lease could not be charged to capital item until it began to produce?

"Mr. Hatcher: The thing I wanted to know is, when it was used in the system and began to affect the return.

"A. That particular field has been used in the system the last two years. The $20,000 item, I cannot say definitely whether that is the portion in Kansas or in Missouri.

"Q. What is that item?

"A. Construct gas pipe line from Ottawa, Kansas, to serve Missouri towns.

"Q. What is the job order?

"A. B-12828, amounting to $20,000.

"Q. You don't know the date?

"A. The line from Ottawa to Sedalia was constructed in the summer and fall of 1930.

"Q. The gas was turned in some time in the fall?

"A. Turned in in the fall of 1930. The next item, of any consequence, is $197,000, rearrange lines to compressor station near Drumright. That station was erected in the fall of 1930 and has been in operation since.

[fol. 596] "Q. What was the job order?

"A. B-12881. The next is $46,000, construct 32 miles of 20 inch line from Dilworth to South end of Wichita 16 inch line. That line was also constructed in 1930 and has been in operation ever since, B-12982. The next item is $87,000 install two 1000 H. P. Units, Higgins compressor station. Those units were installed the same time the units at Wichita, B-12893, installed in the summer and fall of 1930, have been in operation ever since. Item of $224,000, lay 34 miles of 6 inch line, 29 miles of 4-inch line, 12 miles of 3-inch line, 6 miles of 2-inch line, Carson County, Texas. I cannot identify the lines from this description here, B-12929. These lines were laid not later than the 1st of January, 1931.

"Q. All about the same date?

"A. They were all laid on the same job order, gathering lines to the wells in the Carson county field.

"Q. Will you give us the date when the gas was turned into the lines, that is, the approximate date?

"A. No, sir, I do not have any idea I could find the exact date the gas was turned into those lines. There would be no date kept of it. An item of 172,000, replace St. Joe 16-inch line between Lawrence and Tonganoxie, Kansas, B-12960. That work was delayed and was not completed, I believe, until this summer. However, it replaced a previously existing line. This is the cost of the new line: item of $43,000, install motor gas compressor at Ottawa station.

I cannot give you the date on that. It was at least prior to a year ago. There is an item of $49,000, drill and equip Freyler Well No. 2, Noble County, Okla. There has been an exhibit put in on that, it will give the job order and the information on that. There is an item of $32,000, job order B-13129, drill and equip Harris No. 1 well, Seminole County. I think the date of completion of that well would be shown in Mr. Black's valuation. These are the only items of any consequence in this list.

[fol. 597] "Q. Did you have any uncompleted construction of importance on September 1, 1931?

"A. We probably had some open job orders at that time.

"*A.* I am speaking now of the unfinished construction, property not in use?

"A. No, sir, no major items of construction were under way at that time.

"Q. Were there any wells drilled in 1931?

"A. I cannot say.

"Q. Can you tell us, Mr. Eastman, the amount of gas that has been stored in the Craig field?

"A. No, sir, I can tell you approximately, something in excess of a billion feet.

"Q. When was it put in?

"A. At various times during the last two years.

"Q. Have you used any of the storage gas from the Craig field?

"A. Yes, sir.

"Q. Do you know how much has been taken out?

"A. No, sir, in total, it is put in and taken out at different times throughout the year.

"Commissioner Hill: Mr. Eastman, I can see where it would be material if you spent, say, $2,000,000 in 1931 for new construction, for property being constructed, and only part of that became in use during that year if at the same time, you were asking a rate return upon that entire $2,000,000.00 for that year. I think that is the point, I guess you see that too. What we would like to know, if possible, is how much of that amount was used and useful during the year 1931?

"A. That is what I have tried to testify to, Mr. Hill. I can testify that practically all of it was used and useful during 1931 for this reason: In 1931 we have done scarcely

any construction work. The construction work was done during the year 1930.

"Commissioner Hill: Probably would not be $2,000,000.00 worth, there would be some, but you cannot tell us what amount that is?

[fol. 598] "A. I believe—I do not believe any of this $2,000,000.00 carried in this list of uncompleted job orders was—the work was actually done later than 1930. I have been able to identify all the larger amounts in here as to the year 1930. * * *"

"Mr. Hatcher: Our only purpose was to find out what property was not used and useful over the period covered by the investigation and affected by the return, and if the facts show the contrary evidence, we will do nothing. That is why I object to Mr. Hamilton's question.

"Mr. Stone: All of these items were shown to be used and useful in September, 1931, which is assumed to be the rate base. I wondered if you were merely going back for the purpose of income and outgo statements for 1930, or if you wish to take it from the general rate base.

"The Witness: May I answer that previous question? Included in this list is the cost of construction of Drumright station, Mr. Black has inventoried the Drumright station and deducted for accrued depreciation on both buildings and on the equipment.

"Mr. Hatcher: The only objection I had to Mr. Hamilton's question, he made an assumption which is not based on any fact, because we were simply trying to get at the actual condition that existed there, that is all, if it is there and used over the full period, it can be considered in the rate base.

"Mr. Stone: I was merely tryng to get at the purpose of the examination. I do not understand you quite answered my question, yet, on it.

"Mr. Hatcher: The only thing we had in mind was this. If there is property included in this rate base which was not used and not reflected in the return over that period covered, it should not be included so far as the rate of return is concerned.

[fol. 599] "Mr. Stone: Then it makes it quite important to put in, as we did yesterday, the income and outgo for the year 1931, if there would be any question about it being counted.

"Commissioner Hill: But having put that in, this other matter seems to be rather important as to whether all this property valued is used or useful over the period for 1931.

"Mr. Stone: This shows it was all in there a year and used and useful over the period for 1931, and therefore it was in the income and outgo in that statement of 1930, under Mr. Hatcher's theory.

"Commissioner Hill: As I see it, it is a question whether or not this $2,000,000 investment or expenditure for construction was in use during all of the year 1931. Now, under your amended exhibit, you show what your net earnings from operations were in 1931, for the entire year. You had a valuation of the date while it is really July 1st down to September 1st, now if this $2,000,000.00 is included in the valuation and a part was not in use during 1931, I can see where it would be material as to the amount not in use.

"Mr. Stone: This evidence shows, as shown here by this examination, all of it was in use all of the year 1931, except some, possibly some very minor items. That is why I was emphasizing that fact.

"Mr. Hatcher: That is why I cannot understand why you assume we are going to use it, if we get contrary information.

"Commissioner Hill: If the commission, at this time had to pass upon that proposition, we would be somewhat in the air, because we would have to say out of this $2,000,000.00, the evidence shows that a great amount or a big [fol. 690] part of it has been used and useful, or has been used during the year 1931, but we could not say specifically how much.

"Mr. Stone: Mr. Eastman's testimony goes to $1,678,000, which is shown to have been used during the whole year, 1931, out of the $2,000,000.00 and the others are minor items which may or may not, he is unable to testify to. I think that clarifies the situation. * * *"

[fol. 691] "No witness other than Eastman testified as to the matters covered by the above testimony.

"On rehearing, Eastman testified that all property included in Black's and Hamilton's valuation was in use during the entire year ending June 30, 1932.

"'In arriving at the average values the Commission took into consideration net additions to fixed capital from July 1,

1931, to September 1, 1931, amounting to $1,362,586, which is the total net additions shown on Exhibit 91 less the items of leaseholds and leasehold development costs shown thereon.

"The net additions from January 1, 1931, to June 30, 1934, taken into consideration by the Commission in arriving at the average values amounted to $777,591, which is the total of the additions during that period as shown by Exhibit 51, amounting to $993,970.59, less the items of leaseholds and leasehold development costs aggregating a net amount of $180,379.

"The net additions during the six months period ended December 30, 1930, and during the six months period ended June 30, 1931, are the net additions shown on Exhibit 51 covering those periods less the items of leaseholds and leasehold development costs.

"The item of leaseholds and leasehold development costs were omitted from the net additions because the leasehold values were added to the average values separately at the value found by the Commission, to wit: $2,274,200.00.

"The amount of uncompleted job orders was not deducted in any manner by the Commission in arriving at the average values.

"The book value of the plant and property of the company is included in two accounts, to wit: "Plant and Investment" and "Uncompleted Job Orders."

"The book value of the plant and property of the company including completed and uncompleted projects was as follows:

[fol. 6021] January 1, 1930:

Plant and Investment Account	[illegible]
Uncompleted Job Orders	[illegible]
Total	[illegible]

December 31, 1930:

Plant and Investment Account	[illegible]
Uncompleted Job Orders	[illegible]
Total	[illegible]

June 30, 1931:

Plant and Investment Account	$96,795,538.93
Uncompleted Job Orders	2,208,457.57
Total	$99,003,996.50

"The investment in plant and property increased during the six months period ended June 30, 1931, $238,532, and it increased during the twelve months period ended December 31, 1930, $11,675,447."

Rate of Return

The following agreed statement is the evidence submitted to the District Court on the rate of return:

"Testimony in regard to a proper rate of return was given by the witnesses F. C. Hamilton, P. McDonald Biddison and Charles F. Clark for respondents and by C. H. Montgomery for the Commission.

"F. C. Hamilton is a member of the Executive Committee of Henry L. Doherty & Company and in charge of the Rate and Valuation Department of that company; P. McDonald Biddison is a gas engineer of national reputation who testified that he had had many years' experience in financing gas properties; Charles F. Clark, associated with Halsey Stuart & Company of Chicago, testified that he had spent practically his entire business life in intimate touch with the financial operations of the largest industries of the United States; C. H. Montgomery a certified public accountant of twenty years experience, had served for two years on the Kansas Public Service Commission, and from [fol. 603] his experience was familiar with financing matters.

"The witnesses Hamilton, Biddison and Clark, all testified that under existing economic conditions a fair rate should be in excess of 8% and that neither at this time nor in the immediate future could it be hoped that capital could be attracted to a project such as that of the Cities Service Gas Company for a return of 8% but that a much greater return would be required if capital could be interested at all.

"The witness Montgomery testified that a reasonable rate of return for the Cities Service Gas Company would be between 6% and 8% and further testified as follows:

"Q. You stated in your judgment 8 per cent was the amount in normal times that would interest capital?

A. A maximum of 8 per cent in normal times.

Q. Are times very abnormal now?

A. They are, very, at this time.

Q. Do you think you could interest capital in a project of this sort at 10 per cent now?

A. It might be difficult to interest capital under any conditions right at this time.

Q. Wouldn't you say, then that under present conditions 8 per cent would be the minimum?

A. If this project was being initiated at this time, it would be difficult. If such a proposition would be initiated under these conditions, it would be difficult to secure capital at a reasonable amount, if it was contemplated that these conditions would continue for an indefinite length of time.

Q. Well, suppose we are approaching this property as of September 1, 1931. Was the condition at that time any different than what it is now? Was the condition any different on September 1st, the date we have chosen for this reproduction, than it is now?

A. That would depend. Any change in condition probably has been for the worse.

Q. These financial experts have been seeing rainbows in the sky, have they not?

A. They are still seeing them in the future, but conditions have probably become worse since September 1st.

Q. Well, what do you say? Is 8 per cent as of September 1, 1931, an unreasonable rate of return?

A. If it was contemplated that those conditions would last indefinitely and if in view of those conditions anyone would have the courage to go out and embark on such an enterprise, they would probably expect to receive a higher rate than 8 per cent." • • •

[fol. 604] "Testimony was introduced to the effect that because of the assistance of the holding company, the Cities Service Company, the Cities Service Gas Company has been able to sell its securities at an 'interest rate that was from a half to three-fourths per cent less than anything else that was put out at about that time on a similar project,' and in addition to that it gets better terms on its mortgages. It

does not have to pay them off in ten years as many of the pipe line companies have had to do with issues that have been put out in the last two years. Because of this, the Cities Service Gas Company was able to sell its 5½ per cent bonds for 96¼.

'The company, having ample financial resources, does not necessarily have to issue securities now or six months from now, or two years from now. They pick and choose their time when the markets are right.'

"Montgomery's Exhibit 49 shows the financial history of the pipeline system under consideration beginning with the organization of the Cities Service Gas Company to date. The Cities Service Gas Company was organized in the latter part of 1926, acquiring the assets and assuming the liabilities of the following companies:

Empire Natural Gas Company.
Kansas Natural Gas Company.
Empire Gas and Pipe Line Company.
Kansas-Oklahoma Gas Company.
Empire Gas & Fuel Company (Delaware) (Gas properties only).

"The stock control of these companies had been theretofore acquired by Cities Service Company and their assets were acquired and liabilities assumed by the Cities Service Gas Company as of November 30, 1926. Balance sheets of the companies at the time of consolidation are shown on pages twenty-four and twenty-five of Montgomery's Exhibit 49.

[fol. 605] "These balance sheets show that at the date indicated the book value of the plant investment of the companies, including uncompleted job orders, was $52,182,525.98, and that reserves for depreciation and depletion had been accumulated out of earnings in the amount of $22,423,936.95. These reserves which had been accumulated out of earnings amounted to 42.97 per cent of the plant investment.

"These balance sheets show that the companies had accumulated a surplus amounting to $14,903,660.21, which sum is equal to 87.26 per cent of the total capital stock of the companies taken over.

"The combined reserves for depreciation and depletion and surplus amounted to $37,327,597.16, which is equal to

218.55 per cent of all outstanding capital stock of the companies and 71.53 per cent of the plant investment.

"In the case of the Empire Natural Gas Company, it had a capital stock of $10,574,000 and compared to such capital stock it had surplus of $6,066,436 and reserves for depreciation and depletion of $10,192,715, a total of surplus and reserves of $16,259,151, which is equal to 158.77 percent of its capital stock.

"The plant investment of the Empire Natural Gas Company, including uncompleted job orders, as reflected in the books of the company as of November 30, 1926, was $26,577,355; its reserves for depreciation and depletion amounted to $10,192,715, which is equal to 38.35 per cent of the plant investment.

"In the case of the Kansas Natural Gas Company it had a capital stock of $6,000,000 and surplus of $7,784,067 and had accumulated reserves for depreciation and depletion amounting to $11,905,381. Its surplus amounted to 129.73 per cent of its capital stock and the combined surplus and reserves amounted to 198.42 per cent of its capital stock. The book value of its plant investment was $18,861,223, including uncompleted job orders, and its reserves for depreciation and depletion of $11,905,381 was 63.12 per cent of such plant investment.

[fol. 606] "The Empire Gas and Pipe Line Company had a capital stock of $5,000 and surplus of $907,323, which was 18,146.46 per cent of its capital stock. Its reserve for depreciation and depletion was $325,840, making the combined reserves and surplus $1,233,163, all of which was accumulated on a capital stock of $5,000.

"The plant investment of the Empire Gas and Pipe Line Company, including uncompleted job orders, was $1,625,569, compared with combined surplus and reserves of $1,233,163.

"The financial history of the company since the consolidation in November, 1926, may be found on pages 1 to 8, inclusive, in Exhibit 49, which reflects the combined operations of the Cities Service Gas Company, the Cities Service Gas Pipe Line Company and the American Pipe Line Company.

"It is shown there that surplus has been accumulated, in excess of all interest and dividends paid, of $9,044,629 to June 30, 1931; its depreciation and depletion reserves have

increased to $10,818,020. Its total assets have increased from $60,595,001 as of December 31, 1926, to $100,431,039 as of June 30, 1931.

"The Cities Service Gas Company has during all this time paid interest on its bonds and dividends on its capital stock; in 1928 it paid $1,000,000 dividends, and in 1929 and 1930 it paid $2,000,000 each on dividends, which is at the rate of 8 per cent per annum. Its earnings before interest and depreciation were as follows:

1927	$5,330,739
1928	6,053,021
1929	8,000,702
1930	8,899,480
Twelve months ending June 30, 1931	8,741,809

"The net profit of the companies, after paying all interest charges available for reserves and common stock during each of the years 1927 to 1930, was:

[fol. 607]

1927	14.00%
1928	13.12%
1929	21.26%
1930	19.07%

"Its net return after paying all interest and other charges and providing substantial allowances for depreciation and depletion amounted to the following percentages of its outstanding capital stock during each of the years 1927 to 1930, inclusive:

1927	9.06%
1928	6.75%
1929	14.53%
1930	10.82%

"Page 1 of Exhibit 49 shows that the book value of plant investment, including uncompleted job orders, increased from $53,243,128 as of December 31, 1926, to $99,003,996 as of June 30, 1931, an increase of $45,760,868."

Exhibit 49 introduced by Montgomery for the Commission shows that the book value of the plant investment account represents the value at which the property of the company was placed on its books at the time of the con-

solidation in 1926 plus net additions since that time. The value at which the property was placed on the books in 1926 was the aggregate of the book value of the respective properties consolidated including the property of the Kansas Natural Gas Company. The annual reports of the Kansas Natural Gas Company filed with the Department of State of the State of Kansas for the years ending December 31, 1921 introduced as Exhibit 8 and December 31, 1922, introduced as Exhibit 9, show the resources, liabilities, capital and reserves of this company at the above stated dates as follows:

	December 31, 1921	December 31, 1922
Total Resources	$12,922,834.61	$23,443,210.00
Liabilities	1,785,551.21	2,572,838.63
Capital Stock	7,700,250.00	6,000,000.00
Surplus	748,522.54	1,568,243.84
Reserves	2,687,510.86	13,302,128.53
Total Liabilities, Capital and Reserves	$12,922,834.61	$23,443,210.00

[fol. 608] "Total Resources" includes the book value of plant investment which was $11,241,229.97, at December 31, 1921 and $20,389,857.72 at December 31, 1922, an increase of $9,148,627.75.

No new capital was paid in; the combined capital and surplus was less at December 31, 1922 than it was at December 31, 1921.

Hypothetical Pipe Line

"George I. Rhodes testified that he was vice-president and chief engineer of Ford, Bacon & Davis, Inc., a nationally known firm of engineers with headquarters in New York and principal office in Philadelphia, Cleveland, Chicago and San Francisco and offices through which properties are managed in Monroe, Louisiana, Amarillo, Texas, and Colorado Springs, Colorado; that he graduated from Massachusetts Institute of Technology in 1905, and has been continuously engaged in engineering work ever since; that he is familiar with the construction of gas pipe lines and has been engaged in the designing and construction of

such lines for approximately eight years, such work including examination of properties and proposed projects both as to pipe lines and gas reserves; that he was employed by Hamilton and Creveling (of Henry L. Doherty & Company) to make an estimate of the money that would be required to construct a pipe line to take gas solely from the Amarillo field and deliver it to the wholesale delivery points now served by the Cities Service Gas Company and allied companies and also to estimate the amount and cost of gas reserves in connection therewith; that the gas reserves were purely hypothetical "because none of us had any idea that the requisite amount of gas could at this time be purchased and it was therefore necessary to assume that the amount of available acreage in the field would be great enough so that a reasonable reserve—that a purchase of [fol. 609] required reserves could be made without cornering the market, so to speak"; that the proposed hypothetical pipe line is shown by Exhibit 13, a map with the lines projected thereon; that Exhibit 14 is a report showing the estimated cost; that the lines are platted "as the crow flies, rather than taking the actual topography into consideration"; that the lines have been designed as cheaply as could be done; that the quality of service has been reduced from that of the present system; that the system was designed to make an aggregate delivery of approximately 325,000,000 cubic feet of gas per day maximum; "we considered that it would require a reserve of 250,000 acres which we assumed would be pretty well scattered over the field with a correspondingly large gathering system"; * * * "We estimated that the total amount of funds required to acquire the reserves and construct and put the system into operation would be $91,500,000."

"On cross-examination the witness testified that the hypothetical system is comparable to the present system in that it will serve the same markets; that no check of the present system was made to find out whether it had more or less capacity; that the hypothetical system differs in that it has a single source of supply and that a larger number of towns are served with but a single line to them; that the hypothetical system is "somewhat less than the equipment of the present system"; that no consideration was given to gas supplies in Kansas and Oklahoma; that in de-

signing an actual project any available gas closer than Texas would be taken into consideration; that the witness did not attempt to design a project contemplating any supply of gas from Kansas or Oklahoma and could not estimate the difference in price without refiguring the entire project; that the witness is familiar with gas lease prices but is prohibited from testifying in that regard on account [fol. 610] of commitments to other clients; that 250,000 acres of leases could not be bought in Texas at the present time; that $11,000,000.00 was estimated as the probable cost of 250,000 acres or $44.00 an acre. The witness testified that he had no personal knowledge of company's present pipe line system.

Exhibit 14 by Ford, Bacon & Davis, as to cost of hypothetical pipe line introduced by the Company is as follows:

"As requested we have briefly investigated a suggested natural gas system to produce gas solely in the Amarillo Gas Field and to transport and deliver it economically and dependably to the wholesale delivery points and city gates to which gas is now being delivered by the system of the Cities Service Gas Company.

"We have designated such a system having the following characteristics and normal estimated costs:

Present Net Daily Delivery Capacity which can be extended as required to meet growth of the system	325,000 M c. f.
Annual Delivery at present capacity and current seasonal variations in demand	78,600,000 M c. f.
Preconstruction and Organization Cost including engineering and geological investigations and reports on economics and stability of project, earning capacity, etc., the organization of a Company to carry out the project and the negotiation of basic contracts necessary to have in hand before considering the financing of the project	$1,250,000
Financing Cost exclusive of discount on securities but including the cost of negotiations, preparation of extensive financing reports, cost of legal expenses, taxes, etc. involved in the issuance of securities	250,000

Gas Reserves sufficient to insure at least a 20 years' supply of gas with reasonable growth in load taken at a conservative estimate of the gas content of acreage. 250,000 acres minimum in proven territory	11,000,000
[fol. 611] Gas Wells fully equipped, sufficient in number to supply and measure the maximum daily requirement and to protect acreage from migration of gas. 150 producing wells	5,000,000
Gathering System from all wells to a centrally located field compressing station comprising lines from 4 inches to 24 inches in diameter. 272 miles	3,530,000
Gasoline Plant sufficient to strip 325,000 M. F. C. of gas daily with 1,500,000 gal. storage and laid out for convenient extension	600,000
Field Compressing Station sufficient in capacity to compress gas from 200 pounds to 450 pounds gauge and to minimize in the compressed gas all moisture that can condense in the lines, the station having normal spare capacity. $17,500 horsepower	1,870,000
Main Pipe Lines comprising two parallel inter-connected lines 24 inches as far as Wichita Junction, thence 22 inches to Kansas City, the double lines being required to give service approaching that possible with the present system with its multiple lines and sources of gas. 920 miles of pipe	29,310,000
Five Main Line Compressing Stations to repressure the gas in the lines to 450 pounds as required to transport the maximum requirements of gas through the main line, each station having normal spare capacity. 51,250 horsepower	5,210,000

Branch Pipe Lines from 2 inches to 20 inches in diameter to reach the various wholesale points of delivery and city gates, each line having sufficient capacity to meet reasonable expectation of growth in demand.	
2,024 miles	17,630,000
235 Regulator and Meter Stations at points of wholesale delivery and city gates	1,060,000
[fol. 612] Telephone System connecting the field with all compressing stations and principal wholesale delivery points, comprising two circuits along the main line and a single circuit along major branch lines.	
1,735 miles of circuit	730,000
Miscellaneous Property comprising shops, warehouses, garage, automotive equipment, maintenance and repair equipment and other miscellaneous items of property	1,520,000
Engineering and Supervision Costs including preparation of detail designs and specifications, negotiations for purchase of materials and equipment and for construction contracts, inspection and supervision of manufacture of materials and of construction work	3,870,000
Interest During Construction based on a 24 months' construction period	5,060,000
Taxes, Insurance and Other Corporate Overheads during the construction period	2,110,000
Working Capital	1,500,000
Estimated Total amount of funds required to acquire reserves and to construct and put the system into operation	$91,500,000

We hand you herewith a map showing the suggested system, with the following title:

"Cities Service Gas Company. A suggested natural gas system to produce gas in the Amarillo gas field alone and to deliver the gas to present wholesale delivery points."

This map shows the suggested extent of acreage and number of wells required in the Amarillo Gas Field, the suggested location, size and number of pipe lines, the suggested location, size and number of compressing stations and the approximate location of the principal whole-sale points of delivery.

A further investigation and consideration of the suggested system might be expected to refine its design, to adapt it more specifically for the service now possible from the system of the Cities Service Gas Company, to support the estimates of cost with confirming data and details and [fol. 613] to supplement them with estimates of the cost of gas delivered.

Intercorporate Relations

The following agreed statement as to intercorporate relations was presented to the District Court:

"Henry L. Doherty owns over 35 per cent of the voting power of the Cities Service Company and with two exceptions the rest of the stock is in the hands of scattered individuals.

"The common stock of the following distributing companies, respondents herein, is owned by the Gas Service Company with the exception of the qualifying directors' shares: Arkansas Valley Gas Company, Capital Gas and Electric Company, Girard Gas Company, Hutchinson Gas Company, Newton Gas Company, Union Public Service Company, Pittsburg Gas Company, Western Distributing Company, Wichita Gas Company, and Wyandotte County Gas Company.

"The common stock of the Cities Service Gas Company, which sells the gas at the city gates to distributing companies now under investigation, with the exception of directors' shares, is owned by the Empire Gas & Fuel Company. All of the voting stock, with the exception of the directors' shares of the Empire Gas & Fuel Company is owned by the Cities Service Company.

"All of the stock of the Cities Service Gas Pipe Line Company, except qualifying directors' shares, is owned by the Cities Service Company.

"All of the stock, except qualifying directors' shares, of the American Pipe Line Company is owned by the Cities Service Gas Company."

[fol. 614] STIPULATION AS TO CONDENSED STATEMENT OF EVIDENCE

The parties to the above entitled action, by their respective attorneys, stipulate and agree that the foregoing is a true and correct condensed statement of all the evidence introduced before the court in the trial of said action, material to the issues presented on appeal.

This 5th day of May, 1933.

Chas. D. Welch, Louis R. Gates, Chas. W. Steiger, Roland Boynton, Atty. General; E. H. Hatcher, Attorneys for Appellants. Robt. D. Garver, Robert Stone, Attorneys for Appellees.

[fol. 615] IN UNITED STATES DISTRICT COURT

ORDER APPROVING CONDENSED STATEMENT OF EVIDENCE

The foregoing condensed statement of the evidence introduced before this court, having been stipulated by counsel for the respective parties to be correct, the same is hereby approved and settled as correct this 15th day of May, 1933.

Orie L. Phillips, Geo. T. McDermott, Circuit Judges.
Richard J. Hopkins, District Judge.

[File endorsement omitted.]

[fol. 616] IN UNITED STATES DISTRICT COURT

PRÆCIPE FOR TRANSCRIPT OF RECORD—Filed May 15, 1933

To the Honorable F. L. Campbell, Clerk District Court of the United States for the District of Kansas, First Division;

In the certified transcript of the record in the above entitled cause to be made and transmitted to the Supreme

Court of the United States pursuant to an order allowing appeal, dated April 19, 1933, signed by Orie L. Phillips and George T. McDermott, Circuit Judges, and Richard J. Hopkins, District Judge, kindly incorporate the following:

1. Bill of Complaint for injunction filed by the Wichita Gas Company, No. 1637 N, and all exhibits attached thereto including the opinion and orders of the Public Service Commission for the State of Kansas; and the Bill of Complaint for injunction filed by the Cities Service Gas Company, No. 1646 N. All other petitions in the consolidated cases are similar in form and need not be included;

2. Answer filed by defendants in answer to the petition filed by the Wichita Gas Company, No. 1637 N, and the Cities Service Gas Company, No. 1646 N;

3. Request for convening of three judge court;

4. Order consolidating cases;

5. Opinion and findings of the District Court and supplemental memorandum;

6. Dissenting opinion and findings of Hon. Richard J. Hopkins, District Judge;

7. Final decree, or order of the District Court;

[fol. 617] 8. Order substituting parties defendant;

9. Appellant's petition for appeal to the United States Supreme Court, assignment of errors and prayer for reversal;

10. Jurisdictional statement;

11. Order allowing appeal;

12. Copy of bond on appeal;

13. Citation to appellees with return thereon;

14. Acknowledgement of service of appeal papers;

15. Condensed statement of the evidence;

16. This praecipe.

Chas. D. Welch, Louis R. Gates, Chas. W. Stoiger, Roland Boynton, Atty. General; E. H. Hatcher, Attorneys for Appellants.

Received copy of the foregoing praecipe this 5th day of May, 1933.

By Robt. D. Garver, Robert Stone, Attorneys for Appellees.

[File endorsement omitted.]

[fol. 618] Clerk's certificate to foregoing transcript omitted in printing.

[fols. 619 & 620] In United States District Court

[Title omitted.]

[fol. 621] Order Extending Time to File Transcript of Record on Appeal. Filed in U. S. Supreme Court May 26, 1933

For good cause shown, it is by the Court ordered that the time for filing transcript of record on appeal in the Supreme Court of the United States in the above entitled causes, be and the same is hereby extended for a period of thirty days from and after May 29, 1933.

Geo. T. McDermott, Circuit Judge.

[fol. 621½] [File endorsement omitted.]

[fols. 622 & 623] In Supreme Court of the United States

[fols. 624 & 625] Statement of Points to be Relied upon and Designation of the Parts of the Record to be Printed. Filed May 31, 1933

Come now the appellants and adopt their assignments of error as their statement of points to be relied upon, and represent that the whole of the record as filed is necessary for the consideration of the case.

Chas. H. Welch, Louis R. Oates, Chas. W. Steiger, Roland Boynton, Atty. General; E. H. Hatcher, Counsel for Appellants.

Service of copy of the above notice is hereby acknowledged this 27 day of May, 1933.

Robert D. Garver, Robert Stone, Counsel for Appellees.

[fol. 626] [File endorsement omitted.]

Endorsed on cover: File No. 37,717. Kansas D. C. U. S. Term No. 114. The State Corporation Commission for the State of Kansas, Homer Hoch, Jesse W. Greenleaf, et al., appellants, vs. The Wichita Gas Company, The Hutchinson Gas Company, The Newton Gas Company, et al. Filed May 31, 1933. File No. 114, O. T., 1933.

(4080)

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SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1933

No. 114

THE STATE CORPORATION COMMISSION FOR THE STATE OF KANSAS, HOMER HOFF, JESSE W. GREENLEAF, ET AL., Appellants,

vs.

THE WICHITA GAS COMPANY, THE HUTCHINSON GAS COMPANY, THE NEWTON GAS COMPANY, ET AL.

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE DISTRICT OF KANSAS.

STATEMENT AS TO JURISDICTION.

MAY IT PLEASE THE COURT:

The appellants in support of the jurisdiction of this Court to review the above entitled cause on appeal respectfully represent:

In

A.

Statutory Provision Sustaining Jurisdiction.

The Act of February 13, 1925, Chapter 229, Section 1, 43 Stat. 938 (United States Code, Title 28, Section 345), provides that Section 238 of the Judicial Code is amended to read in part as follows:

> "Sec. 238. A direct review by the Supreme Court of an interlocutory or final judgment or decree of a district court may be had where it is so provided in the following sections, and not otherwise:
>
> * * * * * * *
>
> (3) Sec. 380 of this Title."

Section 380 of said Act, being Sec. 266 amended of the Judicial Code, reads in part as follows:

> "No interlocutory injunction suspending or restraining the enforcement, operation, or execution of any statute of a State by restraining the action of any officer of such State in the enforcement or execution of such statute, or in the enforcement or execution of an order made by an administrative board or commission acting under and pursuant to the statutes of such State, shall be issued or granted by any justice of the Supreme Court, or by any district court of the United States, or by any judge thereof, or by any circuit judge acting as district judge, upon the ground of the unconstitutionality of such statute, unless the application for the same shall be presented to a justice of the Supreme Court of the United States, or

> to a circuit or district judge, and shall be heard and determined by three judges of whom at least one shall be a justice of the Supreme Court or a circuit judge, and the other two may be either circuit or district judges, and unless a majority of said three judges shall concur in granting such application. * * *
>
> An appeal may be taken direct to the Supreme Court of the United States from the order granting or denying, after notice and hearing, an interlocutory injunction in such case. * * *
>
> The requirement respecting the presence of three judges shall also apply to the final hearing in such suit in the district court; and a direct appeal to the Supreme Court may be taken from a final decree granting or denying a permanent injunction in such suit."

The Act of February 13, 1925, Chapter 229, Section 8, 43 Stat. 940 (U. S. Code, Title 28, sec. 350), reads in part as follows:

> "No writ of error, appeal or writ of certiorari intended to bring any judgment or decree before the Supreme Court for review shall be allowed or entertained unless application therefor be duly made within three months after the entry of such judgment or decree * * *."

B.

Date of Decree and Date of Application for Appeal.

The decree sought to be reviewed was entered on the 28th day of January, 1933.

The application for appeal was presented on the 19th day of April, 1933.

C.

Nature of Case and Ruling Below.

This is an appeal from the decision of a statutory three-judge court convened in the United States District Court for the District of Kansas, First Division.

The Cities Service Gas Company, a Delaware corporation, is engaged in the business of producing and transporting gas from Texas and Oklahoma and delivering it to distributing companies along its line, among which are the following in the State of Kansas: The Wichita Gas Company, The Hutchinson Gas Company, The Pittsburgh Gas Company, The Capital Gas & Electric Company, The Newton Gas Company, The Girard Gas Company, The Wyandotte County Gas Company, The Union Public Service Company, and The Western Distributing Company.

The common stock of each of such distributing companies, except the qualifying directors' shares, is owned by the Gas Service Company, a corporation. The stock of the Gas Service Company, except the qualifying directors' shares, is owned by the Cities Service Company, a Delaware corporation. The stock of the Cities Service Gas Company, except the qualifying directors' shares, is owned by the Empire Gas & Fuel Company. The stock of the Empire Gas & Fuel Company, except the qualifying directors' shares, is owned by the Cities Service Company.

The Western Distributing Company is a West Virginia corporation and a citizen of that State. The Union Public Service Company is a Delaware cor-

poration and a citizen of that State. The other distributing companies are Kansas corporations.

The Cities Service Gas Company furnishes gas to the distributing companies at the city gates under day to day contracts, which are oral, at forty cents per thousand cubic feet. Each of the distributing companies has contracted to pay Henry L. Doherty & Company one and three-fourths per cent of its gross revenue, a per diem charge and expenses for certain specific services, and an engineering fee of five per cent of the cost of new construction, in consideration of which Henry L. Doherty & Company maintains legal, managerial, engineering, accounting and purchasing staffs whose services are available to the distributing companies.

Each of the distributing companies has also entered into a contract with the Gas Service Company under which the latter furnishes and the former pays for certain services. This contract has been approved by the Commission and is not in controversy on appeal.

On July 2, 1931, the Public Service Commission commenced a proceeding against the corporations hereinbefore named, except the Cities Service Company and the Cities Service Gas Company. It found that the reasonableness of the contracts hereinbefore referred to, and the charges made for services and commodities furnished thereunder, should be inquired into and a determination made of the amounts which properly should be set up as operating expense of the distributing companies on account of expenditures made for such commodities and services under such contracts,

and entered an order on such findings for a hearing to inquire into the reasonableness of such contracts and charges, and directed that respondents in such proceeding furnish such information concerning such contracts as the Commission might desire, and "show cause why such holding company contracts, or service or commodity charges, should they be found to be unreasonable, should not be disallowed as operating expense of the distributing companies, and adjustment made in this respect as to charges made to the consumers."

The Public Service Commission assumed jurisdiction to inquire into the reasonableness of the contracts under the authority expressed in the case of *Smith* v. *Illinois Bell Tel. Co.*, 282 U. S. 133, and *Western Distributing Company* v. *Public Service Commission of Kansas*, 285 U. S. 119.

After a hearing the Commission, on July 20, 1932, made findings to the effect that any amounts paid by the Distributing companies under their contracts with Henry L. Doherty & Company were unreasonable, and that any amounts paid by the distributing companies to the Cities Service Gas Company for gas in excess of 29.5 cents per thousand cubic feet at the city gates were unreasonable, and ordered that on and after August 1, 1932, the distributing companies (1) cease setting up on their books as operating expenses the one and three-fourths per cent payments to Henry L. Doherty & Company and any payments for gas to the Cities Service Gas Company in excess of 29.5 cents per thousand cubic feet, (2) give no consideration to

any such payments in fixing their rates to domestic consumers, (3) reduce their rates to their consumers proportionately, pending a final determination of their rates; and show cause on September 1, 1932, why such reductions should not be made permanent.

A petition for rehearing was filed by the respondents setting up fifty-one grounds. A rehearing, limited to one of such grounds, was granted. After such rehearing, the Commission increased its finding of a reasonable charge for gas at the city gates from 29.5 to 30 cents, and with that modification and the necessary changes in dates, on August 31, 1932, re-entered its order of July 20 in the form of two orders.

The material portions of the first of such orders is as follows;

> "That on and after the first day of September, 1932, the distributing companies, respondents above named, shall cease to set up on their books as an expense item any payments made to Henry L. Doherty & Company under the contract above mentioned, because of the one and three-fourths per cent charge, and also any payments made to Cities Service Gas Company for main-line town border gas in excess of 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer.
>
> "That on the 17th day of October, 1932, the distributing companies, respondents above named, appear before the Public Service Commission, at 10 o'clock a. m., and show cause to the Commission why the reduction in expenses as above set forth should not be passed on to the

consumers with such other reductions as may be found reasonable."

The material portion of the second of such orders is as follows:

> "It is therefore by the Commission ordered, that effective September 1, 1932, and until a hearing is held and an order issued, that the distributing companies, respondents above named, shall charge rates to the consumers as follows:
>
> "All distributing companies paying a gate rate in excess of 30 cents per M. c. f., shall deduct the difference between what the distributing company is now paying at the city gate and 30 cents per M. c. f. and pass on this difference to the consumer."

The nine distributing companies and the Cities Service Gas Company brought separate suits in equity to enjoin the enforcement of the two orders of August 31, 1932. The Public Service Commission of the State of Kansas and Jesse W. Greenleaf, Thurman Hill and C. W. Campbell, as members of said Commission, and Roland Boynton, Attorney General of the State of Kansas, were made parties defendant.

These actions were commenced on September 19, 1932, within the thirty-day period required by Sections 66-118, Revised Statutes of Kansas 1923.

The several bills alleged diversity of citizenship as to the Cities Service Gas Company, The Western Distributing Company and The Union Public Service Company, and alleged that the orders are confiscatory of plaintiff's property, impair the obligation of their

contracts, deny to them the equal protection of laws, and unconstitutionally interfere with interstate commerce.

An application was made for a temporary injunction. At the hearing thereon, the Commission confessed that the second order made on August 31, 1932, was in conflict with Section 66-118, Revised Statutes of Kansas 1923, which prescribes that an order cannot become effective until thirty days after it is entered, and consented that the enforcement of such second order might be permanently enjoined. A temporary injunction was granted against the enforcement of both orders.

The cases were consolidated for trial. Upon the trial the evidence introduced before the Commission was received in evidence, supplemented by an agreed abstract of such evidence, and by stipulation and other evidence.

The case was heard by the statutory three-judge court on the 10th day of November, 1932. The case was taken under advisement and on the 5th day of January, 1933 Judge Phillips handed down an opinion and finding of fact concurred in by Judge McDermott. The opinion and findings of fact increased the valuation or rate base as found by the Commission from $73,170,510 to $82,380,583. The opinion and findings decreased the net income available for return on investment as found by the Commission from $6,769,936 to $5,860,327. The majority court further found that on these calculations the company would be making but 7.11 per cent and the reduction of 10 cents as ordered by the Commission would reduce the rate

of return to 4.8 per cent which it found to be confiscatory.

On the 14th day of January, 1933, Judge Hopkins handed down findings of fact and dissenting opinion holding that the order of the Commission was reasonable and supporting the findings of the Commission with but a few immaterial exceptions as to the valuation and net earnings.

On the 28th day of January, 1933, the statutory three-judge court, for the District of Kansas, First Division, entered its decree in part as follows:

> "That the defendants, the Public Service Commission of the State of Kansas, and the members thereof, and Roland Boynton, Attorney General of the State of Kansas, and each of them, their agents, servants, and employees, and all other persons acting under or through their authority, be and they are hereby permanently enjoined and restrained in the enforcement and execution of the provisions of two certain orders of said Public Service Commission dated August 31, 1932, insofar as the said orders require that the distributing companies, plaintiffs in the above named cases, should cease to set up on their books any payments made to Cities Service Gas Company for main line town border gas in excess of 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer; and, insofar as they and/or either of them require that effective September 1, 1932, and until a hearing is held and an order issued, the said distributing companies should charge rates to the consumers as follows:

> "All distributing companies paying a gate rate in excess of 30 cents per M. C. F. should deduct the difference between what the distributing companies were then paying at the city gate and 30 cents per M. C. F., and should pass this difference to the consumer."

Said decree did not enjoin the Appellants from enforcing the order as to the payment of the 1¾ per cent to Henry L. Doherty & Company, and this appeal is only from that part of the decree enjoining the enforcement of the orders of the Commission as to the gate rate for gas at 30 cents per M. C. F.

After the entering of said decree the 1933 Legislature of the State of Kansas, abolished the Public Service Commission of Kansas, and recreated the same as the State Corporation Commission of Kansas, and by said act the terms of office of Jesse W. Greenleaf, Thurman Hill and F. E. McMullan, successor to C. W. Campbell, expired and Homer Hoch, Jesse W. Greenleaf and Ernest E. Blincoe succeeded them as members of the State Corporation Commission.

That on the 19 day of April, 1933, the said District Court made an order substituting the said the State Corporation Commission and Homer Hoch, Jesse W. Greenleaf and Ernest E. Blincoe as members thereof as defendants in place of the defendants, the Public Service Commission of Kansas and Jesse W. Greenleaf, Thurman Hill and C. W. Campbell.

D.

Cases Believed to Sustain Jurisdiction.

The following decisions of this Court are believed to sustain jurisdiction of this appeal:

In *Herkness* v. *Irons*, 278, U. S. 93, 73 L. Ed. (U. S.) 198, it was decided that the District Court has jurisdiction of a bill challenging the validity under the Federal Constitution of an order of the State Administrative Board and that the Supreme Court has jurisdiction on direct appeal.

See, also, *Oklahoma Natural Gas Company* v. *Corporation Commission of the State of Oklahoma*, 261 U. S. 290, 67 Law Ed. (U. S.) 659; *Western Distributing Co.* v. *Public Service Commission*, 252 U. S. 283.

We respectfully submit that the Supreme Court of the United States has jurisdiction of this appeal by virtue of the sections of the judicial code herein set out.

Respectfully submitted,

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LOUIS R. GATES,
CHAS. W. STEIGER,
E. H. HATCHER,
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Atty. General,
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The Supreme Court of the United States

OCTOBER TERM, 1933.

No. 114.

THE STATE CORPORATION COMMISSION FOR THE STATE OF KANSAS, HOMER HOCH, JESSE W. GREENLEAF, ET AL.,
APPELLANTS,

vs.

THE WICHITA GAS COMPANY, HUTCHINSON GAS COMPANY, NEWTON GAS COMPANY, ET AL.,
APPELLEES.

BRIEF ON BEHALF OF APPELLANTS.

OPINIONS OF THE COURT BELOW.

The majority findings and opinion of the Court below and the findings and dissenting opinion of Judge Hopkins, are reported in 2 Fed. Supp. at page 792. They appear in the record of this proceedings at pages 277-361.

RULE 12.

Rule 12, paragraphs one and two, has been complied with and this court has held it has jurisdiction to entertain the appeal.

STATEMENT OF THE CASE.

This is an appeal from the findings and decree of a statutory three judge court convened in the United States District Court for the District of Kansas, First Division, consisting of Orie L. Phillips, C. J., George T. McDermott, C. J., and Richard J. Hopkins, D. J.

The decree granted a permanent injunction against the Public Service Commission. The matter had been submitted upon the issues joined by the bills of complaint, (R. 1-247), and the answers thereto. (R. 251-266) The bills of complaint all attack the same order of the Commission and were similar in all particulars. Therefore, only the bill of complaint of the Wichita Gas Company and the Cities Service Gas Company and the answers thereto were set out in the record, as the cases were consolidated for trial and treated both in the court below and on appeal as a single case covering a single issue. (R. 249-251)

The Cities Service Gas Company, a Delaware corporation, is engaged in the business of producing and transporting gas from Texas, Oklahoma and Kansas and delivering it to distributing companies along its line, among which are the following in the State of Kansas: The Wichita Gas Company, The Hutchinson Gas Company, The Pittsburg Gas Company, The Capital Gas and Electric Company, The Newton Gas Company, The Gerard Gas Company, The Wyandotte Gas Company, The Union Public Service Company, and The Western Distributing Company.

The common stock of each of such distributing companies, excepting the qualifying directors shares, is owned by The Gas Service Company. The stock of the Gas Service Company, excepting the qualifying directors shares, is owned by The Cities Service Company, a Delaware corporation. The stock of the Cities Service Gas Company, excepting the qualifying directors shares, is owned by The Empire Gas and Fuel Company. The stock of The Empire Gas and Fuel Company, excepting the qualifying directors shares, is owned by the Cities Service Company. (R. 538)

The Western Distributing Company is a West Virginia corporation and a citizen of that state. The Union Public Service Company is a Delaware corporation and a citizen of that state. The other distributing companies are Kansas corporations. The Cities Service Gas Company furnishes gas to the distributing companies at the city gates under a day to day contract, which is oral, usually at 40¢ per thousand cubic feet. In some instances it is less, making average of 39.5 cents (R. 294). Each of the distributing companies has contracted to pay to Henry L. Doherty & Co., 1 and ¾ per cent of its gross revenue, a per diem charge and expenses for certain specific services, and an engineering fee of 5 per cent of the cost of new construction, in consideration of which Henry L. Doherty & Co. maintains legal, managerial, engineering, accounting and purchasing staffs, whose services are available to the distributing companies. The Commission disallowed the 1 and ¾ per cent item as an unreasonable and unnecessary

expense. This finding was not disturbed by the District Court, has not been appealed from by the companies and therefore is not in controversy on appeal. (R. 300)

Each of the distributing companies has also entered into a contract with the Gas Service Company under which the latter agrees to furnish and the former to pay for certain services similar in nature to those contracted for with Henry L. Doherty & Co. The Commission found that one such contract was reasonable, and having disallowed the one with the Henry L. Doherty & Co., approved the contract with the Gas Service Company. Therefore, this contract is not in controversy on appeal. (R. 77)

On July 2, 1931, the Public Service Commission commenced a proceeding against the corporations hereinbefore named, except the Cities Service Company, and the Cities Service Gas Company. It found that the reasonableness of the contracts hereinbefore referred to, and the charges made for services and commodities furnished thereunder, should be inquired into and a determination made of the amounts which properly should be set up as operating expenses of the distributing companies on account of expenditures made for such commodities and services under such contracts, and entered an order on such findings for a hearing to inquire into the reasonableness of such contracts and charges, and directed that respondents in such proceeding furnish such information concerning such contracts as the Commission might desire, and

"show cause why such holding company contracts or service or commodity charges, should they be found unreasonable, should not be disallowed as operating expense of the distributing companies, and adjustment made in this respect as to charges made to the consumers." (R. 26)

The Public Service Commission assumed jurisdiction to inquire into the reasonableness of the contracts under the authority expressed in the case of Smith v. Illinois Bell Telephone Co., 282 U. S. 133, and Western Distributing Co. v. Public Service Commission of Kansas, 285 U. S. 119.

The hearing was commenced before the Commission on October 16, 1931, and closed February 16, 1932. During this time, the Commission heard testimony for twenty six full days and received 101 exhibits, some of the exhibits containing several thousand pages. There was testimony from 40 witnesses and the evidence, when finally transcribed, consisted of 2,991 pages of testimony.

After the submission of the briefs, the Commission, on July 20, 1932, made findings to the effect that any amounts paid by the distributing companies under their contracts with Henry L. Doherty & Co. because of the 1 and ¾ per cent agreement, were unreasonable and not a proper item of expense, and that any amount paid by the distributing companies to the Cities Service Gas Company for gas in excess of 29.5¢ per thousand cubic feet at the city gates, was unreasonable, and ordered that on and after August 1, 1932, the distributing companies should:

1. Cease setting up on their books as operating expense, the 1 and ¾ per cent payments made to Henry L. Doherty & Co., and any payments made for gas to the Cities Service Company in excess of 29.5¢ per thousand cubic feet,

2. Give no consideration to any such payments in fixing their rates to domestic consumers,

3. Reduce their rates to their consumers proportionately, pending a final determination of their rates; and show cause on September 1, 1932, why such reduction should not be made permanent. (R. 182)

A petition for rehearing was filed by the respondents setting up 51 grounds. A rehearing limited to one of such grounds was granted which pertained to the earnings of the Company for the year ending June 30, 1932. After such rehearing, the Commission increased its finding of a reasonable charge for gas at the city gates from 29.5¢ to 30¢, and with that modification and the necessary changes in dates, on August 31, 1932 re-entered its order of July 20, 1932, in the form of two orders. The material portions of the first of such orders is as follows:

> "That on and after the first day of September, 1932, the distributing companies, respondents above named, shall cease to set up on their books as an expense item any payments made to Henry L. Doherty & Company under the contract above mentioned, because of the one and three-fourths per cent charge, and also any payments made to Cities Service Gas Company for main-line town border gas in excess of 30 cents per M. C. F., and should give no con-

sideration to any such payments in fixing a rate for the domestic consumer.

That on the 17th day of October, 1932, the distributing companies, respondents above named, appear before the Public Service Commission, at 10 o'clock A. M., and show cause to the Commission why the reduction in expenses as above set forth should not be passed on to the consumers with such other reductions as may be found reasonable." (R. 59-62)

The material portion of the second of such orders is as follows:

"It is therefore by the Commission ordered, that effective September 1, 1932, and until a hearing is held and an order issued, that the distributing companies, respondents above named, shall charge rates to the consumers as follows:

All distributing companies paying a gate rate in excess of 30 cents per M. C. F., shall deduct the difference between what the distributing company is now paying at the city gate and 30 cents per M. C. F. and pass on this difference to the consumer." (R. 62-3)

The reasonableness of the contracts was tested before the Commission on the basis of the cost of rendering service, plus a reasonable return upon the present fair value of the property used and useful in rendering the service.

The distributing companies and the Cities Service Gas Company brought separate suits in equity to enjoin the enforcement of the two orders of August 31, 1932. The Public Service Commission of the State of Kansas and Jesse W. Greenleaf, Thurman Hill and C. W. Campbell,

as members of said Commission, and Roland Boynton, Attorney General for the State of Kansas, were made parties defendant.

These actions were commenced on September 19, 1932, within the thirty day period required by section 66-118 Revised Statutes of Kansas, 1923.

The several bills alleged diversity of citizenship as to the Cities Service Gas Company, the Western Distributing Company, and the Union Public Service Company, and alleged that the orders are confiscatory of plaintiffs' property, impair the obligations of their contracts, deny to them the equal protection of laws, and unconstitutionally interfere with interstate commerce.

An application was made for a temporary injunction. At the hearing thereon, the Commission confessed that the second order made on August 31, 1932, was in conflict with Section 66-118, Revised Statutes of Kansas, 1923, which prescribes that an order cannot become effective until thirty days after it is entered, and consented that the enforcement of such second order might be permanently enjoined. The temporary injunction was granted against the enforcement of both orders.

The cases were consolidated for trial. (R. 248-250) Upon the trial, the evidence introduced before the Commission was received in evidence, supplemented by an agreed abstract of such evidence, and by stipulations and other evidence. (R. 282)

The case was heard by the statutory three judge court on the 10th day of November, 1932. The case was taken under advisement and on the 5th day of

January, 1933, Judge Phillips handed down an opinion and findings of fact concurred in by Judge McDermott. The opinion and findings of fact increased the valuation or rate base as found by the Commission from $73,170,510 to $82,380,[illegible]. The opinion and findings decreased the net income available for return on investment as found by the Commission, from $6,769,836 to $5,[illegible],327. The majority court found further, that on these calculations, the Company would be making but 7.11 per cent and the reduction of 9.5 cents per M. C. F., as ordered by the Commission, would reduce the rate of return to 4.8 per cent, which it found to be confiscatory.

On the 14th day of January, 1933, Judge Hopkins handed down findings of fact and a dissenting opinion, holding that the order of the Commission was reasonable and supporting the findings of the Commission with but a few immaterial exceptions as to the valuation and net earnings.

On January 16, 1933, the majority Court handed down a supplemental memorandum consisting of an interpretative resume of its former opinion pertaining to the reasonable rate of return.

On the 28th day of January, 1933, the statutory three judge court entered its decree in part as follows:

> "That the defendants, the Public Service Commission of the State of Kansas, and the members thereof, and Roland Boynton, Attorney General of the State of Kansas, and each of them, their agents, servants, and employees, and all other persons act-

ing under or through their authority, be and they are here permanently enjoined and restrained in the enforcement and execution of the provisions of two certain orders of said Public Service Commission, dated August 31st, 1932, insofar as the said orders require that the distributing companies, plaintiffs in the above named cases, should cease to set up on their books any payments made to Cities Service Gas Company for main line town border gas in excess of 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer; and, insofar as they and/or either of them require that effective September 1, 1932, and until a hearing is held and an order issued, the said distributing companies should charge rates to the consumers as follows:

All distributing companies paying a gate rate in excess of 30 cents per M. C. F. should deduct the difference between what the distributing companies were then paying at the city gate and 30 cents per M. C. F., and should pass this difference to the consumer." (R. 361)

Said decree did not enjoin the Appellants from enforcing the order as to the payment of the 1 and ¾ per cent to Henry L. Doherty & Company, and this appeal is only from that part of the decree enjoining the enforcement of the orders of the Commission as to the gate rate for gas at 30 cents per M. C. F. The Appellants objected to and took exception to findings Nos. 13, 14, 16, 17, 18, 19, 20, 21, and to the conclusions of law No. 1, and to that part of the decree which enjoined the Public Service Commission of the State of Kansas in reference to its said orders, and exceptions thereto were allowed. (R. 362)

The Appellants presented their application for appeal, their assignments of error, and bond for appeal on the 19th day of April, 1933, and the appeal was allowed on that date. (R. 367) A condensed statement of the evidence essential to a decision of the questions presented on appeal appears at pages 368 to 539, inclusive, of the record, and a statement of the points relied upon by the Appellants, may be found in the record at page 541.

After the entering of said decree the 1933 Legislature of the State of Kansas, abolished the Public Service Commission of Kansas, and recreated the same as the State Corporation Commission of Kansas, and by said act the terms of office of Jesse W. Greenleaf, Thurman Hill and F. E. McMullan, successor to C. W. Campbell, expired and Homer Hoch, Jesse W. Greenleaf and Ernest E. Blincoe succeeded them as members of the State Corporation Commission.

On the 19th day of April, 1933, the said District Court made an order substituting the said The State Corporation Commission and Homer Hoch, Jesse W. Greenleaf and Ernest E. Blincoe as members thereof as defendants in place of the defendants, The Public Service Commission of Kansas and Jesse W. Greenleaf, Thurman Hill and C. W. Campbell. (R. 362)

SPECIFICATIONS OF ASSIGNED ERRORS.

The errors assigned are as follows: (R. 311)

1. The District Court of the United States for the District of Kansas, First Division, erred in permanently enjoining and restraining the enforcement and execution of the provisions of the two certain orders of The Public Service Commission as dated August 31, 1923, insofar as the said orders require that the distributing companies, plaintiffs in the above cause, should cause to set up on their books any payments made to The Cities Service Gas Company for manufactured town border gas in excess of 30 cents per M. c. f., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

2. The Court erred in refusing to dismiss the plaintiff's bills of complaint and in granting the petitioners any relief.

3. The Court erred in their opinion and findings declaring the order of The Commission was, as to any part, unreasonable and would, if not enjoined, confiscate the property of these plaintiffs.

4. The Court erred in not accepting the finding of facts, declarations of law and dissenting opinion of Honorable Richard J. Hopkins, as declaratory of the law and facts controlling in this case.

5. The Court erred in finding:

> "The present values are on the extensive construction of the last few years, less than the prudent investment therein * * * " (Finding 13.)

6. The Court erred in finding the rate base to be $[illegible] (Finding 14.)

7. The Court erred in finding the present value of The Ohio Fuel Gas Company's rights of way to be $1.02 per rod and erroneously increased the valuation in the amount of 22 cents per rod on rights of way, a total increase of $[illegible] (Finding 14; Account 1307, 1327.)

8. The Court erred in adding $24,318 to the cost of gas well construction as found by the Commission. (Finding 14, Account 1312), and thereby erroneously increased the rate base in said amount.

9. The Court erred in adding $387,011 to the value found by the Commission for production field line equipment, (Finding 14, Account 1344), and thereby erroneously increased the rate base in said amount.

10. The Court erred in finding that the Hogshooter compression station was used and useful, and in adding to the value found by the Commission, $2,100 for land at the Hogshooter station, $43,560 for compression station, and in adding the value of the equipment at the Hogshooter station in the amount of $414,927. (Finding 14, Accounts 1325, 1328, 1331.)

11. The Court erred in finding that the value found for Account 1333 by the Commission should be increased from $39,432,331 to $40,232,331, because the amount of rock excavation in the pipe line construction allowed by the Commission was too low. (Finding 14.)

12. The Court erred in finding that going concern value should be placed in the rate base at $5,000,000.

and the value found by the Commission increased $3,000,000. (Finding 14.)

13. The Court erred in finding that 1,261,000 acres of gas leases owned by The Cities Service Gas Company were used and useful, and should be included in the rate base including developed, proven, probable and prospective acreage, and erred in increasing the acreage allowed as used and useful and in valuing the same at $5,727,272. (Finding 14.)

14. The Court erred in finding that the net income available for return amounted to only $5,860,327, and in including a portion of the rate expense of the present investigation as a proper item of expense in arriving at the net earnings available for return. (Finding 16.)

15. The Court erred in allowing $329,917 as annual replacement requirements on account of rentals on non-producing leases. (Finding 16.)

16. The Court erred in finding that $174,747.74 was necessary as an annual allowance for dry hole expense. (Finding 16.)

17. The Court erred in its finding and conclusion that The Cities Service Gas Company is earning an annual return of only 7.11 per cent on the present valuation of its property. (Finding 17.)

18. The Court erred in its finding and conclusion that approximately 8 per cent return upon present valuation is necessary for The Cities Service Gas Company at the present time, and that a return substantially lower than that would be confiscatory; and erred in its find-

ing that if abnormality is considered, the return must be increased and not decreased. (Finding 18.)

19. The Court erred in its finding that under the orders of the Commission, the return upon the property of the Ohio Natural Gas Company dedicated to the public use would be 4.8 per cent, and erred in its finding that such rate under present conditions is confiscatory. (Finding 19.)

20. The Court erred in its finding that if the distributing companies are compelled to pay 40 cents per thousand cubic feet for gas at the city gates and to base their rates to consumers upon the gross fixed as reasonable by the Commission, no one of them will have earnings in excess of operating expenses applicable to depreciation and return. (Finding 20.)

21. The Court erred in its conclusion of law that that portion of the first order of the Commission, made August 31, 1912, providing that the distributing companies should give no consideration to the payments for gas at the city gates in excess of 30 cents per thousand cubic feet in fixing the rate for domestic consumers, should be permanently enjoined. (Conclusion of law, 1.)

22. The Court erred in its conclusion that 40 cents per thousand cubic feet for gas at the city gates is a reasonable charge. (Opinion.)

SUMMARY OF ARGUMENT.

The lower Court concluded as to the jurisdiction of the Commission herein as follows:

> "We are of the opinion that the facts here justify the conclusion that the Cities Service Company, together with the Gas Service Company, the distributing companies, The Empire Gas and Fuel Company, and the Cities Service Company, are engaged in a common enterprise, namely, the transporting and furnishing of gas to local concerns; that the Cities Service Company exercises such complete dominion and control over the Cities Service Gas Company and the distributing companies that under the general rules of agency, the Cities Service Gas Company and the distributing companies are mere agencies or instrumentalities of the Cities Service Company; and that in substance and effect the Cities Service Company is, through such agencies, supplying gas to local consumers on demand and is engaged in a local business. If this be true, the Commission had the power to determine the reasonableness of the charge set up as operating expense for gas at the city gates in fixing the local rate. That could only be done by determining a reasonable return to the Cities Service Gas Company for producing, transporting and delivering such gas at the city gates." (R. 286)

The lower Court concluded that it must determine the value of the property of the Cities Service Gas Company used and useful in the business of producing, transporting and delivering gas, the amount of its earnings and a fair return upon such property.

With both of the above conclusions of the lower Court, appellants agree.

Appellants contend:

1. The majority lower Court erroneously increased the value of the property of the Cities Service Gas Company used and useful in its business of producing, transporting and supplying gas to the distributing companies at the city gates, from $73,170,510 as found by the Commission to $82,380,583.

2. The Court erred in its finding that all of the gas leases held by the Company in the amount of 1,262,361 acres were used and useful, regardless of their developed, proven, probable or prospective character.

(a). Of the above leases there were 998,287 acres which the Company classified as prospective only. They were not even known to be capable of producing gas and a large part of them were far removed from the present system.

(b). Of the 1,262,361 acres there were 123,440 acres, proven but not developed, located in the Hugoton field. The Hugoton field is over 90 miles from any pipe line of the present system. A major addition to the present system is necessary to make this field available.

(c). The Company owned 69,367 acres of other leases 24,547 of which was situated outside the proven sweet gas area, some being in the sour gas area and not suitable for domestic consumption, and the remainder is not developed.

(d). The Commission allowed 71,267 acres as used and useful and the evidence given by the Company's own witnesses showed conclusively that within said 71,267 acres there was sufficient gas to last the Company for

over 22 years, on the basis of its requirements for produced gas in 1930.

(e). We contend that the gas leases which a company should be allowed to place in the rate base as used and useful should under no circumstances exceed an amount sufficient to meet the needs of its patrons for a reasonable time in the future. The actual facts as to the gas consumption of the Company's patrons are in the record. The actual facts pertaining to the available gas were carefully calculated by expert geologists for the Company and substantiated by the expert geologists for the Commission. The Company's officers testified that all the leases were acquired as gas reserves for this pipe line and in their judgment were a necessary acquisition. We submit that the assumption of the Company's officers cannot stand against the facts. The excess leases may be a prudent investment for the Company, but they are not used and useful in serving present patrons.

3. The Commission had an opportunity to observe all of the witnesses, went carefully into all of the evidence as shown by its opinion and findings, and the record before the Court below did not disclose any substantial reason sufficient to overcome the presumption that the findings of the Commission were correct.

4. That the majority lower Court erroneously found:

> "Under the present rates, the Cities Service Gas Company is earning 7.11 per cent a year upon the present value of its properties." (R. 317)

5. The majority lower Court erroneously found, contrary to the evidence, that:

> "A return of approximately 8 per cent upon present values is necessary, under present conditions, to assure confidence in the financial soundness of the Cities Service Gas Company, to maintain its credit, and to enable it to raise money necessary for the discharge of its public duties. Any return substantially lower than that would be confiscatory. (United Railways v. West, 280 U. S. 234, 252.)" (R. 317)

There is no evidence that any further financing is necessary. In fact, the evidence shows that the Company is fully financed.

6. That the majority lower Court erroneously construed the law as stated in the West case, supra, when it applied it to the facts in the case at bar.

7. That the majority lower Court in its Finding No. XVIII found that these times are abnormal and then erroneously found that if abnormality is considered, the return must be increased, not decreased. (R. 318) It therefore appears that the lower Court concluded that the more difficult and depressed the times, the more the utility should earn. Developing this conclusion, it would appear that as the ability of the patron to pay decreases, the rate of return of the utility increases.

8. That the majority lower Court erroneously found the net available annual return from such property to be $5,860,327.

(a). The majority lower Court erroneously deducted from net income $329,917 as annual depletion requirements for rentals on nonproducing leases. We contend

that the allowance is improper due to the fact that the Company is carrying 998,287 acres of prospective leases not even known to be capable of producing gas and many so far from the pipe line that they are not accessible to the system. These leases are not useful at the present time, and as we have said heretofore, are entirely in excess of an amount required to meet the needs of its patrons for a reasonable time in the future.

(b). The lower Court erroneously deducted from net income $174,747 as an annual allowance for dry hole expense. The prospective acreage is not useful. In the proven area all of the evidence shows there is little likelihood of encountering a dry hole and in the proven sweet gas area of the Amarillo field, no dry hole has yet been encountered.

The Company now has ample proven gas reserves sufficient to last it for many years in the future and its period of pioneering is past.

9. That the majority lower Court erroneously concluded that 40 cents per thousand cubic feet for gas at the city gates is a reasonable charge.

10. That the majority lower Court erroneously concluded that to compel the Cities Service Gas Company to furnish gas at 30 cents per thousand cubic feet will result in a confiscation of its property.

11. The majority lower Court erroneously failed to give consideration to the fact that earnings had decreased during the test period due to loss of sales of industrial gas.

The value of the service to the domestic consumer has not increased. Where the rate for domestic consumption is attacked as confiscatory, consideration should be given the fact that the decrease in earnings upon which the claim for confiscation is based grew out of loss in industrial sales. A temporary loss created by one class should not be made a burden upon another.

The rights of a particular class of patrons cannot be ignored. A utility should not be allowed to maintain rates that are unjust to one class of its patrons because there has been a temporary loss of income from another. The constitution does not require that temporary loss in income be remedied by imposing an unreasonable burden upon another class of patrons, with no increase in the value of the service. (Covington & L. Turnpike Road Co. v. Sanford, 164 U. S. 578)

12. That the findings of fact, declarations of law and dissenting opinion of the minority lower Court should be declaratory of the law and facts controlling in this case.

ARGUMENT.

JURISDICTION OF THE COMMISSION.

The Court sustained the Commission's finding as to jurisdiction to investigate into the reasonableness of the 40 cent contract, no exceptions were taken thereto and no appeal was taken therefrom. It is believed, however, that a brief discussion of the theory of jurisdiction will throw some light on the findings of the Commission and the Court below, and be helpful in considering the findings as to value and net available annual return.

The Commission assumed jurisdiction under the authority expressed in the recent case of Western Distributing Co. v. The Public Service Commission of Kansas, 285 U. S. 119. In that case the same question existed as to the right of the Commission to require evidence as to the reasonableness of the 40 cent contract. The same holding companies and the same pipe line companies were involved. The Western Distributing Company one of the appellees herein, was the plaintiff and appellant in that case. In that case, the Court said:

> "The appellant adverts to the fact that in its bill of complaint are included a number of averments not denied by the appellees. In brief these are that the company does not own or produce any natural gas; that the only source of supply for the city of El Dorado is the main of the Cities Service Gas Company; that no supply at a lower price can be obtained from any other source; that the same rate is being charged to other distributing companies

> along the lines of the Cities Service Gas Company, and was being charged by another independent pipe line to another city; that an ineffectual effort had been made to find local gas available to El Dorado; and that appellant had attempted to get a lower rate from Cities Service Gas Company, but could not do so. It is urged that as these averments were uncontradicted they constitute, when taken with the facts previously stated, a prima facie case for the reasonableness of the rate charged. This might well be true were it not for the fact of unity of ownership and control of the pipe line and the distribution system. An averment of negotiation and effort to procure a reduction in the wholesale rate means little in the light of the fact that the negotiators are both acting in the same interest, that of the holding company which controls both. All of these facts so averred in the pleadings would be far more persuasive with respect to the propriety of the rate if the parties were independent of each other and dealing at arm's length.
>
> Where, however, they constitute but a single interest and involve the embarkation of the total capital in what is in effect one enterprise, the elements of double profit and of the reasonableness of inter-company charges must necessarily be the subject of inquiry and scrutiny before the question as to the lawfulness of the retail rate based thereon can be satisfactorily answered." (See also Smith v. Illinois Bell Telephone Co., 282 U. S. 133.)

It is admitted by the Appellants that a State Commission cannot fix the price to be charged for natural gas transported from one state to another, sold and delivered in bulk to an independent distributing company. The Commission was of the opinion, however, that the facts here justified the conclusion that the Cities

Service Company, together with the Gas Service Company, the Empire Gas and Fuel Company, the Cities Service Gas Company and the distributing companies are engaged in a joint enterprise for the transportation and furnishing of gas to local consumers, that the Cities Service Company exercises such complete domination and control over the Cities Service Gas Company and the distributing companies that under the general rule of agency the Cities Service Gas Company and the distributing companies are mere agencies or instrumentalities of the Cities Service Company; and that in such status and effect, the Cities Service Gas Company is, through such agencies, supplying gas to local consumers on demand and is engaged in a local business. This opinion of the Commission was supported by finding 5 of the Court below as follows:

"Except for qualifying shares, the common stock of the distributing companies is owned by the Gas Service Company, the stock of which in turn is owned by the Cities Service Company. The common stock of the Cities Service Gas Company is owned by the Empire Gas & Fuel Company, the voting stock of which in turn is owned by the Cities Service Company. The Empire Gas & Fuel Company has a preferred stock issue outstanding in the hands of the public. Henry L. Doherty & Company is Henry L. Doherty, who owns thirty five per cent of the voting stock of the Cities Service Company. The Cities Service Company, by stock ownership, legally controls the policies of the distributing companies and the pipe line company; and Henry L. Doherty in fact controls the policies of the Cities Service Company. The distributing companies do not deal at arm's length with either the Cities Serv-

for the Company or Henry L. Doherty & Company." (R. 205)

It is a well settled rule of law that a state does have power to regulate the price of gas brought into a state and sold directly to consumers because, "the business of supplying on demand local consumers is a local business, even though the gas be brought from another state and drawn for distribution directly from interstate mains, and this is so whether the local distribution be made by the transporting company or by independent distributing companies." (Missouri v. Kansas Gas Co., 265 U. S. 298; Penn Gas Co. v. Pub. Ser. Com., 252 U. S. 23; East Ohio Gas Co. v. Tax Com., 283 U. S. 465.)

It necessarily follows that the Commission had the power to determine the reasonableness of the charges set up as operating expense for gas at the city gates in fixing the local rates. This was done by determining a reasonable return to the Cities Service Gas Company for producing, transporting and delivering such gas at the city gates. The reasonable return was determined by arriving at the value of the property of the Cities Service Gas Company, used and useful, in the business of producing, transporting and delivering gas, the amount of its net earnings and a fair return upon such property.

The alternative, should it be conceded for the purpose of argument that the Commission could only scrutinize and inquire into the reasonableness of such charges

was well stated by the lower Court in its opinion as follows:

> "However, if we grant that the Commission can only scrutinize and inquire into the reasonableness of such contracts, we are of the opinion that the same result necessarily follows. Since the Cities Service Company enjoys a monopoly and affords the only reliable source for supplying gas to the distributing companies, the only method of determining the fairness and reasonableness of the charge at the city gates is to determine the reasonableness of the return to the Cities Service Gas Company on their property used and useful in the business. Any charge in excess of that for gas at the city gates, under the contract between two subsidiary corporations who have the same parent or holding corporation, would be unfair and unreasonable." (R. 287)

The case was tried before the Commission and before the Court below upon the theory that the reasonableness of the contracts should be determined on the basis of a reasonable return to the Cities Service Gas Company for producing transporting and delivering gas at the city gates, and the facts necessary for such determination were presented.

Counsel for the distributing companies, in his opening statement to the Commission, recognized the propriety of the above test of the reasonableness of the pipe line company's charge for gas at the city gate. The opening statement of counsel for the distributing companies was adopted by The Cities Service Gas Company and attached to its bill of complaint as Exhibit "A". We quote from the statement as follows:

"The question in which the Commission should now be interested, and the only issue which we now recognize in this proceeding as far as the city gate rate is concerned, is as to whether or not *the earnings of the Cities Service Gas Company under the existing city gate rate are more than a fair return on the fair value of its property.*" (R. 234)

Again counsel states:

"On whatever value is shown to exist, the pipe line company is entitled to a fair return. It asks nothing more." (R. 235)

Counsel closed his statement as follows:

"We respectfully decline to voluntarily do anything to cripple our ability to continue such service; nevertheless we recognize now and always that we are entitled to only a fair return on a fair value of our property." (R. 236)

CONTENTION OF CITIES SERVICE GAS COMPANY.

The Cities Service Gas Company is the gas pipe line company which supplies gas to the affiliated distributing companies. The intercorporate relations and the Court's findings thereon have been discussed.

In the hearing before the Commission only the distributing Companies were before it as parties because over them the Commission had direct jurisdiction. In the case before the lower Court the Cities Service Gas Company also filed a petition.

The theory of the pipe line company appears to be that even though the Commission had jurisdiction over the distributing companies and made a valid order which

the distributing companies could not attack, the pipe line company could come in and attack the order.

We do not believe the contention has any weight. It was not given any by the lower Court.

The lower Court found against every contention of the Cities Service Gas Company.

The Court in its finding No. 5 found that:

> "The Cities Service Company, by stock ownership, legally controls the policies of the distributing companies and the pipe line company; and Henry L. Doherty in fact controls the policies of the Cities Service Company. The distributing companies do not deal at arms length with either the Cities Service Gas Company or Henry L. Doherty & Company." (R. 295)

No objections were made and no exceptions were taken to the finding.

The Court in its opinion stated as follows:

> "The Commission had the power to determine the reasonableness of the charge set up as operating expense for gas at the city gates in fixing the local rate." (R. 286-7)

The lower Court sustained the Commission's order as to the payments to Henry L. Doherty & Company, in which the same legal questions were involved. (R. 291) The Cities Service Gas Company took no appeal.

By Exhibit A attached to the pipeline Company's bill of complaint, it is conceded that the distributing Companies and the pipe line Company is controlled by the Cities Service Company.

It is stated in the exhibit:

> "The intent of Cities Service Company in the beginning was to confine its activities to the Pipeline end of the business, leaving the distributing companies in the hands of their then owners entirely unassociated with our organization. *** The large markets, such as the two Kansas Cities, Wichita, Newton, Hutchinson and Topeka were owned by corporations unfriendly to the pipe line ownership and had been antagonists in litigation with it for the preceding ten years. *** In the opinion of the officials of the Company, responsible for adequacy of service by the pipeline, the situation was such as to require ownership of the distributing companies in order to assure a market which would greatly increase investment and which was necessary in order to give proper and adequate service to the consumers." (R. 231 2)

It therefore appears that the Company had two purposes in getting control of the distributing plants. One was to get rid of litigation as to the rate being charged by the pipe line Company. The other was to assure a market. If the owners of the pipe line company had control of the distributing companies they would not be going into other markets for cheaper gas.

F. C. Hamilton, consulting engineer for Henry L. Doherty & Co., also testified that the distributing companies were purchased to get rid of litigation and unfriendly relations between the pipeline company and the distributing companies. (R. 455-6)

The only questions presented by the assigned errors and before the Court on appeal, pertain to the valuation of the property, the net income and the rate of return

as affecting the reasonableness of the Commission's order.

EXPLANATION OF ORDER IN WHICH ASSIGNED ERRORS CONSIDERED.

Assigned errors 1, 2, 3, 4, 21 and 22 go to the findings of the Court below which are general conclusions drawn from its findings of the value of the property used and useful in the business of supplying gas to the affiliated distributing companies, and its findings of net available annual return.

Assigned errors 5, 6, 7, 8, 9, 10, 11, 12 and 13 go to the Court's findings as to value of the property used and useful in the business of supplying gas. All of the lower Court's findings as to value were considered under its finding 14. (R. 302)

Assigned errors 14, 15, 16, 17 go to the lower Court's findings of net available annual return.

Assigned errors 18, 19 go to the lower Court's findings as to necessary rate of return.

In order to present the case in the order of its development, the assigned errors will not be considered in their numerical order. We will first consider those going to value, then those going to the net available annual return, those going to the necessary rate of return, and last, those going to conclusions from the basic findings.

THE VALUATION.

Assigned Errors 5, 6, 7, 8, 9, 10, 11, 12 and 13.

Generally.

The question of valuation was gone into very carefully before the Commission. The Commission heard testimony for twenty-six days and received one hundred and one exhibits. Some of the exhibits contained thousands of pages. There was testimony from forty witnesses and the evidence when finally transcribed consisted of 2,901 pages of testimony.

The chief witnesses who testified in regard to the valuation exhibits were: F. D. Hamilton, Consulting Engineer for Henry L. Doherty & Company, and H. L. Eastman, associated with Mr. Hamilton for the respondent and E. B. Black of the firm of Black & Veatch, Consulting Engineers of Kansas City, Missouri, for the Public Service Commission. For convenience these witnesses will be referred to in the brief as Hamilton, Eastman and Black.

All the engineers based their valuations on reproduction cost less depreciation.

In making its findings the Commission had the benefit of having heard the witnesses testify and observed their demeanor. The case was submitted to the court on the evidence submitted to the Commission and other exhibits. There was no oral testimony presented to the lower court.

In weighing the findings of the court and the Commission it may be helpful to give some consideration to

the methods used by the engineers in preparing the inventory and in the valuation of the property.

Black testified that in making the appraisal or fixing prices he did not use rock bottom prices for labor or material, (R. 374) although it was common knowledge that common labor at the time of the investigation could be obtained at thirty cents or less an hour. Black used forty cents for common labor.

Black in testifying concerning the methods used by him in preparing the inventory and valuation of this property said that he started by requesting the various companies concerned to supply specific information such as maps, plans, construction contracts and all other data having to do with the physical property of the Company; that his engineering forces were organized as rapidly as required to make computations and to check the data furnished by the Company; that engineers were put into the field for the purpose of checking location, kind and condition of such parts of the property as could be checked by physical inspection, and to obtain additional data not contained in the information furnished by the company; that engineers were sent out with the company's inspection crews for the purpose of determining the per cent condition of pipe lines where these crews examined them; that he personally made an inspection of the major part of the territory covered by the liens of the company and that in all approximately 20,000 miles was traveled by his engineers and himself in this inspection and checking, and that from the start of this work, July, 1931, until the final compilation of the valuations

from 8 to 19 engineers were working with him either in the field or checking field data, or compiling quantities.

The data furnished Black by the company consisted of pipe-line maps prepared by the company's own engineering department and which were complete with respect to length of line, size of pipe, weight of pipe and such other data as is required for a record of pipe-line construction, and when the maps did not disclose the data necessary they were supplied by the engineering department of the company. On all major structures, such as compressor station buildings, detail plans were furnished by the company, and where such plans were lacking in detail, additional information was obtained by personal inspection in the field. The company's engineers furnished lists of all machinery in compressor station structures and throughout the system, and this was checked in the field by Black's engineers. In the field survey of structures, Black caused photographs to be taken of practically every structure in the system.

Hamilton in his valuation of many of these accounts, as found by the Commission did not go into detail, but contented himself with a general lumping of the accounts, as is shown by his handling of the following accounts:

In account No. 1310, production field measuring station structures, Black's valuation lists 597 of these structures, 554 of which are carried as individual items, each structure being priced out in accordance with Black's testimony (R. 92-3) by separating structures into classes by sizes and type of construction. Detailed estimates of

materials and costs were determined for each class and the cost then applied on a cubic-foot basis.

Hamilton's structures in this account, while listed by individual structures, were not detailed with respect to methods used in determining the cubic-foot costs applied by him.

Eastman testified (R. 96) with respect to account No. 1311, which testimony was applied also to account No. 1310, that no supporting data for his cubic cost development was available.

In account No. 1315, production field measuring station equipment, Hamilton summarized the items entering into this account by gas fields only, and there is no other detail of this account in Hamilton's exhibits other than the total cost of reproduction of these accounts by fields, except on two pages of his exhibit 17A and B where the number and unit prices of meters in the account are detailed, and the Commission had no supporting data offered, nor could it secure such by examination of Hamilton or Eastman from which these accounts could be checked. (R. 101)

In the case of account No. 1329, transmission measuring station structure, Hamilton shows a total valuation of $165,893 new and $155,018 depreciated. This account is shown only by total dollars by states, no detail being given as to the number of structures and no testimony being offered by any of the company's witnesses concerning such totals. (R. 112)

On the other hand, in Black's appraisal in the preparation of unit prices to apply to various units of property,

all items were built up by addition of direct structural overheads applied to labor and materials.

The prices of valves and fittings were determined by discounts from manufacturers' lists, and the prices of pipe were determined by quotations from the manufacturers f.o.b. the mill, or the application of differentials, and the freight to the point of destination added.

Mr. Black introduced as exhibit 42 a unit cost analysis covering 440 pages showing in detail the development of direct structural overheads, of pipe prices, labor, installation prices and prices for various valves and fittings entering into this construction. He also supplied any additional data requested by the company's attorneys and gave a complete breakdown of all unit prices, for materials or labor, as requested. Exhibit 42 and his additional testimony, both on direct and cross-examination, discloses the detail whereby the unit costs used by him were built up, and it is not necessary to go outside the record to obtain all of the detail used by him in obtaining his unit costs. (R. 115)

On the other hand, although the witnesses for the Company had available the complete records of the Company and they could have furnished all details, with respect to the physical items, costs and amount of labor used by them in the development of the company's unit costs, nevertheless, in no case did the company's witnesses give any breakdown of unit costs used by them in determining the value of this property, except in a few cases of pipe-line construction. Their testimony was that they could not go beyond the unit costs shown

in the appraisal, because as they claimed, the supporting data were too voluminous to bring into the hearing room, and no supporting detail from which unit prices were developed or by which they could be tested was ever produced on the original hearing before the Commission, but on rehearing before the Commission an exhibit containing several thousand pages was introduced, purporting to show such breakdown.

Both Black and Hamilton have followed the same classification of accounts, but it is possible that some property classified by Black under account 1314, production field-line equipment, may have been classified by Hamilton under account 1333, transmission line equipment, or vice versa. Black classifies certain rights of way under account 1307, production rights of way, whereas Hamilton places all rights of way under account 1327 transmission rights of way. Both engineers worked with approximately the same inventory of property items, and it is apparent all property has been included by both, in some classifications.

The following summary is a classification of accounts by account number and description except that no account numbers appear for the last seven items. This summary also shows the value as found by the Court and the Commission for the various accounts.

In order that controverted items may be readily ascertained from the summary we have, where the Court's and Commission's findings were the same as to value, indicated the agreement by inserting Id under the Commission's value.

SUMMARY OF COURT'S AND COMMISSION'S FINDINGS AS TO DEPRECIATED VALUE.

Acct. No.	Title of Account	Court	Commission
1307	Production—Right of way	$ 64,778	$ 55,982
1327	Transmission—Right of way	1,915,427	1,657,530
1310	Production—Field measuring station structures	35,909	Id.
1311	Production—Other Structures	47,876	Id.
1312	Production—Gas Well Construction	1,294,710	1,153,157
1313	Production—Gas Well Equipment	658,439	Id.
1314	Production—Field Line Equipment	3,523,176	3,126,159
1315	Production—Field measuring station equipment	265,746	Id.
1332	Transmission—Measuring station equipment	759,625	Id.
1316	Production—Drilling and cleaning equipment	27,908	Id.
1317	Production—Other Equipment	1,333	Id.
1325	Transmission—Land	147,202	145,202
1328	Transmission—Compressing Station Structures	1,515,662	1,466,102
1329	Transmission—Measuring Station Structure	133,310	Id.
1330	Transmission—Other Structures	113,341	Id.
1331	Transmission—Compressing Station Equipment	8,463,835	8,048,910
1333	Transmission—Line Equipment	40,232,331	39,432,331
1334	Transmission—Other Equipment	5,633	Id.
1376	General—Other Land	3,655	Id.
1379	General—Other Structures	94,687	Id.
1380	General—Office Equipment	106,035	Id.
1381	General—Store Equipment	1,805	Id.
1382	General—Shop Equipment	23,084	Id.
1383	General—Stable Equipment	568	Id.
1384	General—Garage Equipment	81,448	Id.
1385	General—Laboratory Equipment	8,202	Id.
1386	General—Telephone and Telegraph System	415,070	Id.
1387	General—Tools and Implements	44,979	Id.
1388	General—Other Equipment	21,832	Id.
	Engineering and Superintendence during construction	3,321,250	2,881,000
	Preliminary and Organization Expense	500,625	480,008
	Administration and Legal Expense during construction	350,350	304,084
	Miscellaneous Construction Expenditures	700,700	608,169
	Taxes during Construction	875,171	778,044
	Interest during Construction	4,471,934	3,883,282
	Working Capital	775,000	Id.
	Materials and Supplies	628,675	Id.
	Gas in Line	22,000	Id.
	Going Concern Value	5,000,000	2,000,000
	Gas Leases	5,727,272	2,874,390
	Rate Base	$82,380,583	$73,170,510

The court increased the total depreciated value as found by the Commission $9,210,073.00.

At the risk of repetition it is believed that it will be helpful to insert here a brief summary of the difference between the Court's and the Commission's findings of value as to the disputed items.

Summary of Disputed Accounts.

1307. PRODUCTION—RIGHT OF WAY.
1327. TRANSMISSION—RIGHT OF WAY.

The Court found that twenty-two cents per rod should be added to the Commission's cost of obtaining rights of way. The Court therefore added twenty-two cents per rod to 39,987 rods of right of way which Black placed under account 1307, increasing the Commission's value $8,796.00.

For transmission rights of way the Court also added 22 cents per rod, but through error computed the same on 1,172,284 rods instead of the agreed figure of 1,114,115 rods. The Court's increase over the Commission's value of this item therefore should have been stated as $249,100 instead of $257,897.

The value placed on the 65,440 rods of telephone right of way was not changed.

1312. PRODUCTION—GAS WELL CONSTRUCTION.

The Court considered 1312 jointly with account 1313 and added to account 1312, $57,235.00 on account of storage wells and $84,318.00 on account of its findings

as to cost of construction, increasing the Commission's value of account 1312, $141,553.00.

1314. PRODUCTION—FIELD LINE EQUIPMENT.

The Court added $397,017.00 to this account because of Black's assumption that field lines were buried only one-half the depth of main lines and therefore the ditching was less expensive.

1325. TRANSMISSION—LAND

The Court found the Hogshooter compressor station used and useful and added $2,000 to the Commission's value for the land.

1328. TRANSMISSION—COMPRESSOR STATION STRUCTURES.

For the same reason mentioned in account 1325, the court added the value of the structure of the Hogshooter compressor station in the amount of $49,560.00.

1331. TRANSMISSION—COMPRESSOR STATION EQUIPMENT.

For the same reason mentioned in account 1325 the court added the equipment at the Hogshooter compressor station in the amount of $414,925.00.

1333. TRANSMISSION—LINE EQUIPMENT.

Without any detailed mathematical calculations the court added $800,000.00 to the Commission's findings as to the value of this account on the basis that the Commission's allowance for the amount of rock excavation was too low as shown by the re-survey made after the

hearing before the Commission. The Court adopted the Commission's findings as to cost of rock excavation but increased the amount of rock to be excavated.

ENGINEERING AND SUPERINTENDENCE DURING CONSTRUCTION.

The Court added $440,250.00 to the Commission's finding as to the value of this account. The Court arrived at the value by applying 5% to the properties except certain items of general equipment as agreed to by the parties. The Commission depreciated this account $337,585.00. The parties have stipulated that overheads should not be depreciated and that no annual allowance for depreciation on overheads should be made. There remains a difference of $102,665 which is accounted for by the fact the Court increased the value to which the percentage was applied.

PRELIMINARY AND ORGANIZATION EXPENSE.

The Court adopted the Commission's finding of ¾ per cent of the value of the physical property but added $20,617.00 because it increased the value of the physical property. The Commission did not depreciate this account.

ADMINISTRATION AND LEGAL EXPENSE DURING CONSTRUCTION.

The Court adopted the Commission's finding of one-half of one per cent of the value of the physical property but added $36,010.00 because the Commission depreciated the account, and $10,256.00 because it increased

the value of the physical property, making a total addition of $46,266.00.

MISCELLANEOUS CONSTRUCTION EXPENSE.

The Court adopted the Commission's finding of one per cent of the value of the physical property but added $72,018.00 because the Commission depreciated the account and added $20,513 because it increased the value of the physical property, making a total addition of $92,531.

TAXES DURING CONSTRUCTION.

The Court adopted the Commission's finding as to this account but used the reproduction new value instead of deducting depreciation, making a difference of $97,127.00.

INTEREST DURING CONSTRUCTION.

The Court adopted the Commission's allowance of 6 per cent but added $468,652.00 because the Commission depreciated the item and $120,000 because it increased the value of the property.

GOING CONCERN VALUE.

The Court added $3,000,000.00 to the Commission's finding as to going concern value.

GAS LEASES.

The Court added $2,852,882 to the Commission's value of gas leases including all leases owned by the Company at cost, regardless of their developed, proven, probable or prospective character.

Presumption and Burden of Proof.

We are mindful of the fact that on the question of confiscation, the plaintiffs below are entitled to an independent judgment as to the law and facts, but in determining these facts, we are of the opinion that the findings of the Commission are presumed to be correct and that the burden is upon the plaintiffs to overcome this presumption. (Blanton v. Belt Line Ry. Corp., 268 U. S. 413, 422; Cotting v. Kansas City Stock Yards Co., 183 U. S. 79; Denver Union Stock Yards Co. v. U. S., 57 Fed. 2d, 735; Los Angeles G. & E. Corp. v. Railroad Commission, 289 U. S. 287, 77 L. ed. 820.)

In weighing the evidence as between the lower Court's and the Commission's findings, it must be kept in mind that the evidence submitted to the lower Court consisted almost entirely of the transcript of the evidence submitted to the Commission, and that the Commission and not the lower Court was the fact finding tribunal which had the opportunity to hear the witnesses testify. There was no oral testimony before the lower Court.

In our following discussion of the facts pertaining to the valuation, we are of the opinion that in no case was the evidence before the lower Court nor is the evidence before this Court, sufficient to overcome the presumptions of the correctness of the Commission's findings.

Accrued Depreciation.

There was no material controversy as to the Commission's finding on accrued depreciation except as to account 1333, transmission—line equipment. The lower

Court disposed of this controversy with the following statement:

> "The Commission found the property to be in 90.1 per cent condition. The Company asserted it to be in 92.93 per cent condition. The Commission's finding is supported by the testimony of its engineer and a consulting engineer called by the Company. We approve the Commission's findings as to per cent condition." (R. 307)

The appellees accepted the Court's finding and there is no controversy as to accrued depreciation on appeal. (R. 416)

Discussion of Disputed Accounts.

The disputed accounts will be discussed in the order in which they appear above.

Assigned Error No. 7.

1307 Production—Rights of Way.
1327 Transmission—Rights of Way.

These two accounts cover rights of way for production and transmission lines and telephone lines used in connection therewith. The two accounts have been treated together for the reason that some controversy has arisen as to how the respective engineers classified particular lines as between production and transmission.

There are in the system 65,440 rods of telephone rights of way which the Commission's engineer Black, priced at 25 cents per rod and the Company's engineer Hamilton, at 15 and 20 cents per rod. There is included in Black's valuation $16,360 for telephone rights of way

and in Hamilton's valuation $12,475. The Commission adopted Black's value for telephone rights of way and there is no controversy as to this item.

As to the number of rods of pipe line rights of way involved in the two accounts, Black calculated 1,212,251 and Hamilton calculated 1,180,102. Black computed his rodage from maps furnished by the Companies, which in error, did not show that certain lines had been reclaimed and abandoned, and the rodage as calculated by Hamilton is correct. (R. 396).

Black testified that the figures used by him in finding the value of rights of way were the result of information procured by his organization from other pipeline companies operating similar lines. The unit costs developed by him were 85 cents per rod on pipe lines under 16 inch and $1.20 per rod for lines of 16 inch and over. (R. 396) His average total cost for all rights of way was $0.997 per rod.

The Company divided the system in nine groups in arriving at the cost of rights of way. The cost per rod in the various groups ranged from $2.11 to $3.54. (R. 397)

The breakdown of the unit price for the group calculated at $3.54 per rod is as follows:

Aerial Surveys	$ .10	per rod
Field Surveys in Staking the Route of the Line	.19	" "
Right of Way Payments for Purchase of Easements from Land Owners	1.25	" "
Crop Damage and Damage to Fences and Trees	.70	" "
Expense of Obtaining Right of Way Agreements	.30	" "
Abstract and Recording of Rights of Way Agreements	.10	" "
Miscellaneous Expense	.10	" "
Clearing, Grading and Fencing	.80	" "
	$3.54	" "

The same items were considered in the breakdown of the other groups but the price applied per unit was less. (R. 397)

It immediately appeared that four of the items were improperly included in the cost of rights of way. They will be discussed separately in the next four paragraphs following.

The cost of Aerial Survey was improperly included because the system was built without it and the advantages were not reflected. (R. 404-5)

The cost of Field Surveys in Staking the Route of the Line was improperly included because both engineers made the allowance under the general account of Engineering and Superintendence by calculating engineering on all the physical property accounts including the ac-

counts covering right of way. To place engineering under rights of way and again under the general account of engineering would be a duplication.

Miscellaneous Expense was improperly included because it was simply thrown in as a possible expenditure with no evidence to support it, and for the additional reason that it was already included under the general account Miscellaneous Construction Expenditures. Miscellaneous Construction Expenditures was calculated on all physical property accounts, including the accounts covering rights of way. To place it under the account for the cost of rights of way and again under the general account for Miscellaneous Construction Expenditures would be a duplication.

The cost of Clearing, Grading and Fencing was improperly included because it is not part of the acquisition cost of rights of way but enters into the cost of construction. Black included the cost of clearing, grading and construction damages under the general construction accounts and there it was allowed by both the lower Court and the Commission. (R. 403-4) Construction contracts were introduced which showed that under the practice of the Company cost of clearing rights of way, etc., was included in the construction contract as part of the construction cost as calculated by Black. (R. 403)

The elimination of the four items just discussed from the Company's right of way cost was approved by the lower Court in the following language:

> "The Company's figure of around $3.00 includes aerial surveys, which were not used, and if used,

> probably would have been worth their cost in a saving not reflected in its present valuation. Apparently the Company also included certain construction costs elsewhere accounted for." (R. 304)

The Commission, in arriving at a value to be placed on rights of way was confronted with the following problem:

Two engineers of national reputation and high standing had presented to the Commission a value to be placed upon rights of way with a difference in their judgment ranging from 85 cents to $3.54 per rod, and the calculations of one engineer containing many apparent improper items.

The Commission then had its accountant, Clinton H. Montgomery, who had made an audit of the books of the Company, prepare an exhibit showing the actual cost of the right of way to the Company.

Montgomery testified that he made an audit of the books of the Company covering 6,215,512 feet of pipe line and that,

> "The rights of way and damage costs totaled $407,179.82 or an average of $1.08 per rod; that the number of rods included in his audit totaled 376,698 or 31 per cent of the total rods included in accounts 1307 and 1327. [The entire system.] (R. 397)

A large part of the system was constructed before the system was acquired by the present Company and its books therefore did not reflect the original cost as to that part.

The 31 per cent reported on by Montgomery was ac-

quired by the present Company during the peak of high prices and the figure of $1.08 per rod should have reflected the highest acquisition cost of the Company.

The Company contended that all the elements of the cost of acquisition of rights of way was not reflected in the figure of $1.08 per rod as shown by the books of the Company. An engineer for the Company testified:

> "The costs of right of way as shown in Exhibit No. 87 are not the entire costs of a right of way on the various lines. As I explained some few days ago, at a previous hearing, these costs include nothing for the acquisition of right of way, which is a major item.
>
> Q. What do you mean by costs of acquisition of right of way?
>
> A. Going out and securing right of way, having it abstracted and recorded.
>
> Q. That is, it does not include the expense of men in the field, the automobiles, phone calls and all that?
>
> A. No, sir; it does not." (R. 402)

The Commission then gave to the exhibit showing the book cost, the most favorable interpretation that could be given to the Company, that was, that none of the costs of rights of way were included in the figures of $1.08 as reflected by the books of the Company, except Rights of way Payments for Purchase of Easements from Land Owners, and Crops Damages and Damages to Fences and Trees. These two items were necessarily reflected in the book cost, if the book cost meant anything, as it was an original cost for the acquisition of rights of way and could pertain to no other property account.

The Commission then eliminated from the items set out by the Company's engineer in making up the rights of way costs, Aerial Surveys, Field Surveys in Establishing Route of Line, Miscellaneous Expenses, and Clearing, Grading and Fencing for the reasons already set out, and allowed items for the cost of rights of way as follows:

Rights of Way Payments for Purchase of Easement, Crop Damage and Damage to Fences and Trees	$ 1.08 per rod
Expense of Obtaining Rights of Way Agreements	.22 " "
Abstracting and Recording	.10 " "
Total	$1.40 " "

In this allowance, the Commission used the book cost for the first two items; used the cost testified to by the Company's witness Hicks for the expense of obtaining rights of way, and used the cost testified to by the Company's engineer for abstracting and recording rights of way agreements.

The Court added 22 cents to the Commission's cost of rights of way, which increased Account No. 1307 $8,796 and increased Account No. 1327 $257,887. The Court stated its reasons therefor as follows:

> "The Commission allowed $1.40 a road for rights of way. It used $1.08 as a basis, that figure being the average cost as shown by the books of the Company of 31 per cent of its rights of way. To this,

the Commission added 22 cents per rod for expense of acquisition and 10 cents per rod for abstracting and recording fees. The evidence clearly developed that the figure of $1.08 did not purport to represent all of the costs and is not a dependable figure. The most dependable evidence is that of a man who negotiated for these rights of way during the past four years. His offering price to all land owners was 50 cents per rod for land and 50 per rod for damages; sometimes he paid as much as $2.00 per rod for land alone; the average damage paid was 65 cents. He did not state the average cost for the land, but it can not be assumed that he acquired all of it at his offering price. It should not be figured lower than 65 cents, the average paid for damage for which his offer was likewise 50 cents. These items make $1.30 per rod paid the land owners, adding to that the 32 cents allowed by the Commission for overhead gives a figure of $1.62, which we have used." (R. 304)

We believe that the lower Court misconstrued the evidence when it found that "the evidence clearly developed that the figure of $1.08 did not purport to represent all of the costs and is not a dependable figure."

It was conceded by the Commission and all parties from the evidence submitted by the Company, that the figure of $1.08 did not purport to represent all of the costs.

The Commission in its findings conceded that it represented none of the overhead costs and for that reason the Commission added to the figure, the cost of Abstracting and Recording Right of Way Agreements and The Expense of Obtaining Rights of Way. The other four items which the Company contended were not included

in the figure of $1.08 were eliminated by the Commission for the reasons already stated.

The lower Court and the Commission are in accord as to the items which should be allowed in the costs. The only conflict therefor remaining between the findings of the Commission and those of the lower Court goes to the figure of $1.08, which makes up the cost of rights of way Payments for Purchasing of Easements and the Cost of Crop Damage and Damage to Fences and Trees.

The Court added to these two items, which the Commission calculated at $1.08, 22 cents, making a total of $1.30 for the two items, stating that:

> "The most dependable evidence is that of the man who negotiated for these rights of way during the past four years. His offering price to all land owners was 50 cents per rod for land and 50 cents per rod for damages; sometimes he paid as much as $2.00 per rod for the land alone. The average damage paid was 65 cents." (R. 304)

With this statement of the Court, we cannot agree. We believe that the most dependable evidence is the actual cost as shown by the books of the Company, and if the estimates made by the man who acquired the rights of way and his oral testimony pertaining thereto conflict with the actual cost figure as shown by the books of the Company, the most dependable evidence is the actual cost shown by the books and not the estimate made by the field man. This appears to us to be in accordance with the lower Court's findings on other

items that estimates and assumptions cannot stand against the actual facts.

In our opinion the lower Court made a mistaken analysis of the testimony as to what costs were not included in the figure $1.08 when it concluded that the figure should be raised to $1.30.

The lower Court, in support of its figure of $1.30, in Finding 14, referred to the testimony of the man who negotiated for the rights of way during the past four years, (Hicks), "That the average damage paid was 65 cents," and then while admitting that the witness did not state the average cost for the land contented itself by asserting that it should not be figured lower than 65 cents and then proceeded to add the two figures, proclaim the result of the addition as being $1.30 and conclude that the land owner was paid such sum.

We respectfully submit that the evidence does not justify an increase of the Commission's finding as to the cost of acquiring rights-of way, and the value pertaining to these two accounts in the amount of $55,982 for Account No. 1307 and $1,657,530 for Account No. 1327.

Assigned Error No. 8.

1312 Production Gas Well Construction.
1313 Production Gas Well Equipment.

The lower Court discussed these two accounts together in its Finding No. 14, and the same procedure will be followed here.

Account No. 1312, Production Gas Well Construction, covers all costs of drilling gas wells and the placing in the wells of all casing, tubing and equipment furnished by the owner. The number of wells, location and the items entering into the account were taken by Black from an inventory furnished by the Company. (R. 96)

Account No. 1313, Production Gas Well Equipment, covers all casing, tubing and fittings going into the wells.

The evidence pertaining to these accounts will be found on pages 377 to 388 of the record.

The lower Court added $141,553 to this joint account, covering $57,235 which the Commission had deducted for so-called storage wells in the Augusta and Craig fields, and $84,318 growing out of the cost of other gas well construction. No addition was made directly to Account No. 1313.

The following table shows the findings by the Commission and the lower Court and the increase made by the lower Court:

Acct. No.	Title of Account	Court	Commission	Increase
1312	Production—Gas Well Construction	$1,294,710	$1,153,157	$141,553
1313	Production—Gas Well Equipment	$ 658,439	$ 658,439	None
	Total Increase			$141,553

We will first consider the addition made by the Court in the amount of $57,235 growing out of the allowance in the valuation of the so-called storage wells in the Craig and Augusta fields. The wells are ones which were formerly drilled for gas and were abandoned after the gas was exhausted. The record shows that the re-

spondents had two fields which they used for storage, one known as the Craig field and the other as the Augusta field. These fields are used as a reservoir into which gas is placed during the summer months when the demand for gas is low, as a reserve to be used during cold weather when the demand is greater. The record shows that the Company, after the gas in the Craig field was exhausted, or depleated to such an extent that production was not profitable, entered into contracts with the land owners whereby they leased these lands containing the abandoned wells for storage purposes. There were 19 of the wells in the Augusta field and 47 in the Craig field. The wells were given a depreciated value of $57,235.

From the evidence introduced before the Commission, it found that the abandoned wells (referring to the hole only), belonged to the land owners and not to the Company and that they were simply leased to the Company for the purpose mentioned in the storage contract and that the Company had no title to them and had no investment in the Craig field wells, and that they should not be included in the valuation of the pipe line company's property. On the basis of this finding, the Commission eliminated the value placed upon the holes from the rate base.

At the hearing before the lower Court, the Company introduced additional evidence which showed that in the Craig field the Company obtained the right to use the abandoned gas wells from the land owners under a stor-

nge contract, which provided that it was to be placed in escrow until the commencement of operation and until the payment of $10 per acre and the payment of his share of the recoverable gas remaining in the storage strata. In connection with this evidence, the Court found:

> "It is not denied that the wells are properly used for storage and for a public purpose; the claim is that the land owner has the property interest in the hole in the ground. Upon the trial before this Court, it was conclusively proven that the Company has entered into gas leases with royalties paid in advance for the use of these wells. Its rights thereto are the same as in producting leases. The assumption of fact made by the Commission is erroneous. The legal conclusion need not be examined." (R. 305)

As yet there are no storage contracts in the Augusta field. The wells there are being used for storage without cost to the Company. These wells are depleated and the Company has already had returned to it, the cost of the hole through amoritization. It might be said as to the storage wells in both the Craig and Augusta fields, that they were worthless when acquired by the Company for other than storage purposes, and nothing was paid the owner for the value of the wells. They were only leased. The only consideration which passed was an annual rent for the use of the field for storage purposes plus a consideration for any immaterial amount of gas that remained in the field. If the wells cost the Company nothing at the time the storage contracts were acquired, it is not reasonable to assume

that the holes would have to be purchased if the pipe line system were reproduced.

The other increase made by the Court in this account may be set out in its own language as follows:

> "The other item is $84,318 growing out of the cost of gas well construction. The Company's figures were considerable below actual cost and below the cost of adjacent wells drilled by other companies of the same depth. The engineer for the Commission omitted certain items in his calculations which may account for his figures being so much below the actual cost of construction. The Commission's figures are so far below the cost of these wells or any other well in the vicinity that they approach the arbitrary." (R. 305)

As to the Court's statement that "the engineer for the Commission omitted certain items in his calculations which may account for his figures being so much below the actual cost of construction", we believe the Court misunderstood the facts pertaining to the situation. In Account No. 1313 pertaining to Gas Well Equipment, Black used the same price for casing and tubing in these wells that he used for the main line pipe of the same weight and size. It was conclusively established that casing and tubing must be purchased from local warehouses and not from wholesale houses as was the pipe in the main line and that therefore a higher price must be applied. For that reason the Commission accepted Hamilton's total price of $853,309 for casing and tubing, corrected for overheads, and eliminated any controversy as to this item. There is no other evidence in the record of the omission of any items. In fact, the record

shows that the number of wells, location and items entering into construction were taken by Black from an inventory furnished by the Company. (R. 96)

The record contains the agreed statement that:

> "To Black's figure for Account No. 1313, the Commission added $236,373 new and $173,925 depreciated because the prices Black applied to casing and tubing in the wells was considered insufficient." (R. 378)

The record further discloses by agreement that if the controversy as to storage wells is eliminated from the accounts the difference between Hamilton's depreciated value and that found by the Commission is but $84,318. (R. 379)

The value of these two accounts amounted to $2,483,068 new and $1,811,596 depreciated, and there was only $84,318 difference between the value placed upon them by the Company and the Commission. Yet the Court finds that, "the Commission's figures are so far below the cost of these wells or any other wells in the vicinity as to approach the arbitrary." (R. 305) Such a conclusion is not possible. The Court was evidently confused by some comparisons made by the Company as to values placed upon the construction by the Commission's engineer before the price of casing and tubing was adjusted by the Commission. In fact, when the adjustments were made the Commission practically conceded to the Company the full value it asked for the account.

The Company owns 304 wells which divided into the difference in value found by the Commission and the Company, amounts to but $275 per well for construction

and equipment. When the cost of these wells, which ranged from $3,000 to over $30,000 each, is considered, a difference between the value found by the Court and as found by the Commission, of approximately $275 per well, can hardly be said to approach the arbitrary. The slight deduction made by the Commission from the Company's value was largely due to the adjustment in overheads which appear justified by the evidence, with nothing in the record to the contrary.

We do not believe it necessary to burden the Court with a lengthy review of the evidence pertaining to these accounts. It is apparent that the lower Court was confused in its reason for making the addition, and in its suggestion that the Commission's finding approached the arbitrary.

Assigned Error No. 9.

1314 Production—Field Line Equipment.

This account covers the labor and materials necessary to construct and test pipe lines between the wells and transmission system. The evidence pertaining to this account will be found on pages 388 to 395 of the record.

There was a disagreement between the engineers for the Commission and the Companies as to the price of pipe going into this account. The Commission eliminated this controversy by adjusting the price of pipe and there was no dispute as to the pipe price before the Court below. The controversy before the Court below consisted of the cost of labor and construction—largely that of

ditching and back filling. The Commission found the value of this account new to be $3,548,102 and the depreciated value to be $3,126,159. The Court added $397,017 to the Commission's depreciated value, stating its reasons as follows:

> "The Commission adopted Mr. Black's estimate, which was based on assumption that field lines were buried on the average to one-half the depth of main lines. The Company's value was based upon the facts. Black testified his figures would have been more accurate if he had had time to gather the facts. It clearly appears also that field lines are more expensive to construct than main lines; they are in smaller units; more hand labor is involved; and more connections are necessary; also the cost of field lines cannot be decreased by taking advantage of the topography as may generally be done with main lines. The Company's figures are strongly buttressed by an analysis of actual cost of field lines utilizing 20,600 tons of pipe. The assumptions of the Commission and its engineer cannot stand against the facts." (R. 305-6)

It is our opinion that the Court, in basing its finding on the criticism of Black's assumption without considering the facts from which the assumption was made, arrived at an entirely erroneous conclusion.

It will be noted that the assumption only went to the amount of ditching and back filling of field lines.

In pricing this account, Black testified that all field lines in Texas up to and including 4 inch, were priced on the assumption that they were buried at one-half the depth of the main line and that in other states field lines up to and including 10 and ¾ inch were assumed as

being placed in trenching one-half the depth of the main line of the same size, and that ditching and back filling was included on the basis of half depths on all lines in consideration of the fact that approximately 872,000 feet of field line are above the ground. (R. 388)

It must first be noted from the statement above that Black only considered lines of 4 inch or under as field lines for the purpose of estimating ditching and back filling in the Texas field. This field is the largest that the Company has. All field lines greater than 4 inch were considered as buried the full depth. After having eliminated all field lines over the size mentioned above for the purpose of calculating trenching at one-half the depth of main lines and considering the fact that 872,000 feet of field lines are above ground, Black's assumption was no doubt correct.

However, we do not need to bore the Court with a detailed discussion of the manner in which Black arrived at his conclusion that field lines should be calculated at one-half the depth of main lines to justify the correctness of his assumption.

If Black's assumption is supported by the findings of the Company's engineers, certainly they are in no position to attack it. If Black's assumption resulted in a figure higher than that asked for by the Company, certainly it is in no position to attack Black's figure. This is the case. The evidence discloses that Black's assumption was in the Company's favor rather than against it, and if the Court made any correction, it should have decreased the allowance rather than increased it.

This is shown by calculating the excavations of field lines allowed by Black and Eastman from their respective exhibits. Black allowed 283,386 cubic yards of earth excavation and 45,389 cubic yards of rock excavation, a total of 328,775 cubic yards. Eastman allowed 261,580 cubic yards of earth excavation, and 44,293 cubic yards of rock excavation, a total of 305,873 cubic yards.

It necessarily results that Black allowed 21,806 cubic yards of earth excavation more than Eastman and 1,096 yards more of classified rock excavation than did Eastman. If Black's assumption, fallacious or otherwise, resulted in an allowance to the Company of 21,806 cubic yards of dirt excavation and 1,096 cubic yards of classified rock excavation more than it asked for and this was allowed by the Commission, we cannot see how the appellees were hurt by Black's assumption, neither do we see how the Court was justified in increasing the Commission's allowance where the assumption resulted in a benefit to the appellees. If the Court made any adjustment because it felt the assumption was erroneous and it desired to accept the Company's figures because the Company's figures were based upon the facts, then the Commission's allowance should have been decreased rather than increased.

The difference between Black's valuation of this account and the valuation of the appellee's engineer, was not due to the fact that Black figured his excavation and back filling for field lines at one-half the depth of the main lines, but rather was due to labor costs after the amount of ditching and back filling was ascertained.

Black's cost for both earth and classified rock excavation was approved and used by the lower Court. In discussing Black's price for classified rock excavation under Account No. 1333 which was the same price used by Black for his classified rock excavation under Account No. 1314, the Court said:

> "Applying Black's price to an increased amount indicated by the test, results in an increase of this item *** ". (R. 308)

Neither did the Court in Account No. 1333 disturb Black's price for earth excavation.

We therefore submit that having approved Black's prices, the Court should have either accepted Black's figures as to the amount of ditching and back filling on field lines, or it should have applied Black's prices which it approved to the amount of ditching and back filling found by the Company, which would have resulted in a reduction of the value of the account instead of an increase of $397,017.00 as found by the Court.

Assigned Error No. 10.

1325 Transmission Land.
1328 Compressor Station Structures.
1331 Compressor Station Equipment.

The Court increased the valuation found by the Commission for Account No. 1325 Transmission Land $2,000.00, Account No. 1328 Compressor Station Structures $49,560.00, Account 1331 Compressor Station Equipment $414,925.00. (Finding No. 14, R. 306)

These represent the value of the land, structure and

equipment of the Compressor Station at Hogshooter, Oklahoma, and should not be added to the valuation of these accounts as found by the Commission, unless the Commission was not justified in its determination that Hogshooter Station was not in use and was abandoned.

Counsel for the State contend that the evidence supports the Finding of the Commission that the Hogshooter Station was not in use, and was abandoned on September 1, 1931, and that it was error for the Court to increase these accounts.

The evidence shows that the Hogshooter Station was not in use on September 1, 1931, the date of the valuation, but was then abandoned and had been abandoned probably for five years and has contributed nothing to the earnings of the system during the period covered by the investigation; that this station had been constructed in 1909, and was acquired by the Company when it took over the old Kansas Natural property; that the gas field it was intended to serve had become exhausted; that the lines to this Station were coupled with the old style dresser coupling, not capable of withstanding the high pressure under which the Company now operates. It is true that on February 3, 1932, Mr. Eastman testified that the Hogshooter Station was at that time useful to the Company and that it was the intention of the Company to weld the 18 inch line extending north from this Station so that it would be capable of carrying high pressures, and that a requisition for that work had been prepared, and that when

this was done the Station would be capable of use; however, the testimony also showed that on February 3, 1931, the Company made a tax return to the Oklahoma Tax Commission, with reference to this Station, stating for the purpose of obtaining a reduction of its taxes:

> It "is now and has been abandoned for several years. This property is now subject to sale and reclaim and has only a junk or salvage value of not to exceed $5,000.00." (R. 406)

In view of all of this testimony, we submit that the finding of the Commission that this Station was not in use and abandoned, should be sustained and that the finding of the Court as to these three accounts should be diminished by the said amounts added for the value of the land, structure and equipment of the Hogshooter Station.

Assigned Error No. 11.

1333 Transmission—Line Equipment.

This account covers the transmission pipe line of the Cities Service Gas Company in place, including both material and labor. The evidence pertaining to this account will be found on pages 415 to 443 of the record.

The Commission found the reproduction cost new of this account to be $43,746,298, and the reproduction cost new less depreciation to be $39,432,331.

Without any detailed mathematical calculation, the Court added $800,000 to the Commission's finding as to the depreciated value of this account on the basis that

the Commission's allowance for the amount of rock excavation was too low as shown by the resurvey made after the hearing before the Commission.

This account made up approximately half of the total valuation of the properties in dispute. At the hearing before the Commission there was a dispute between the engineers pertaining to this account on the price of pipe, the percentage condition of the property, the price to be applied to rock excavation, and the amount of rock excavation in the system. The Commission eliminated the dispute as to the price of pipe by adding $589,960 to Black's price of pipe. It was agreed by the parties before the District Court that:

> "The addition of $589,960 made by the Commission to the value found by Black covers pipe and paint, the Commission having found the value of the pipe in the system to be $26,931,305, which for the purpose of this case will be accepted by the parties." (R. 415)

As to the remaining disputes pertaining to this account, it was agreed by the parties before the District Court as follows:

> "The remaining difference between the value for the entire account as found by the Commission and that as claimed by Hamilton, is accounted for by the difference in percent condition found by Black and adopted by the Commission, and the percent condition claimed by Hamilton and by the difference in estimates by Black and Hamilton as to the amount of rock excavation in the system and the price to be applied to such rock excavation." (R. 416)

The Court disposed of the controversy existing as to the per cent condition as follows:

> "The Commission found the property to be in 90.1 per cent condition. The Company asserts it to be in 92.93 per cent condition. The Commission's finding is supported by the testimony of its engineer and a consulting engineer called by the Company. We approve the Commission's finding as to per cent condition." (R. 307)

The Court also adopted Black's excavation prices and applied them to the amount of rock excavation.

It has been agreed by the parties, for the purpose of this appeal, as follows:

> "For the purpose of this appeal, the parties have agreed to accept per cent condition found by the Court and the unit cost which the Court found should be applied to rock excavation, leaving in dispute only the amount of rock excavation to which the agreed price should be applied." (R. 416)

Therefore, the only controversy pertaining to this account remaining for discussion is the amount of rock excavation. Black used a price of $2.50 per cubic yard for classified rock excavation, which included both pick and shoot rock. (R. 438) Eastman used a price of $7.38 per cubic yard for shoot rock excavation, and $4.01 per cubic yard for pick rock excavation. (R. 434) Black's price has been approved by the Court and agreed to by the parties, Eastman's price which he valued for the appellees, is so far out of line that a comparison by dollars and cents would be of little or

no value. The argument will therefore be presented on a cubic yard basis.

The controversy pertaining to the amount of rock excavation was stated by the Court as follows:

> "There is a difference between the engineers as to the amount of rock excavation in the lines. After the hearing before the Commission, engineers for both sides drilled a hole every quarter of a mile along a main 125 miles long. That extensive investigation developed that the per cent of rock excavation was 20.94 per cent instead of 10.46 per cent used by Black. If over cuts are included, the per-cent is 28. We are inclined to believe that over cuts should be excluded. It is probable that contracts for trenches would be predicated on the trench depth and would not call for over cuts caused by the inability to blast to a neat line. This additional evidence convinces us that Black's estimate of the amount of rock excavation is too low. His estimate on the line used for the test was 24,000 yards; Hamilton's was 72,482 yards. The test showed on Black's own figures exclusive of over cut, 46,790 yards." (R. 307)

From the evidence before the Commission and upon which it made its findings, there was nothing to justify disturbing the Commission's findings as to the amount of rock excavation necessary in trenching for main lines.

Following the hearing before the Commission and pending the trial of the case before the lower Court, the appellees, accompanied by engineers for the Commission, made the resurvey and the drilling test mentioned by the Court. The test was made on a line 125 miles long and weighed by the Court against the estimate of

the engineers on over 3,000 miles of pipe line in the system as a whole.

According to Black's figures developed from the resurvey or drilling test, his estimate for the amount of rock in the 125 mile line was a little less than half what the test showed, while Hamilton's estimate was approximately twice what the test showed. According to the Court's calculation on the resurvey as shown by the quotation from its opinion above, the rock excavation on the 125 mile line was 20.94 per cent. Black having allowed but 10.48 per cent, his estimate as shown by the test was 10.48 per cent too low. On the other hand, Hamilton had used 31.15 per cent for the amount of rock excavation in the 125 mile line. The new survey or drilling test on the Court's calculation having shown that the amount of rock excavation in the line was 20.94 per cent, it necessarily results that Hamilton was 10.11 per cent too high. In other words, Hamilton, in estimating the amount of rock excavation on the 125 mile line, was approximately as much too high as Black was too low, if the resurvey was to be used as a test of the accuracy of their estimates. The Court, in its opinion, stated further:

> "The subject is not capable of exact proof, but we are of the opinion that Mr. Black's amount of excavation should be materially increased. Mr. Hamilton's valuation of rock excavation is $4,211,120. Mr. Black's $1,270,117, of which $1,154,503 is in this account. Applying Black's price to an increase amount indicated by the test results in an increase of this item from $39,432,331 to $40,232,331." (R. 307)

The addition which the Court made to the depreciated value of this account because it found Black's calculation as to the amount of rock excavation to be too low, was $800,000.

The Court and the Commission found the per cent condition of this account to be 90.1 per cent. Reducing the depreciated value which the Court added, ($800,000) to the value new before depreciation for the purpose of finding the exact number of cubic yards which were added by the Court, we arrive at $887,888.

The Court adopted Black's price for rock excavation and as was shown from the quotation from the record previously made herein, this price was agreed to by the Company. Black's price for rock excavation was $2.50 per cubic yard. Dividing the $887,888 added by the Court to the value new before depreciation, by $2.50, the cost of rock excavation, we find that the Court added 355,155 cubic yards of rock excavation to Black's allowance. Black allowed 508,046 cubic yards of rock excavation. (R. 434.), adding to that the 355,155 cubic yards additional found by the Court, gives us a total amount of 863,201 cubic yards of rock excavation which the Court allowed for this account, which covered the excavation for main lines. Hamilton's total allowance of rock excavation for this account was 834,289 cubic yards. (R. 434) Comparing this with the allowance made by the Court because of its addition, we find that the Court allowed 28,912 cubic yards of rock excavation more than that asked for by the Company and estimated by Hamilton.

The test showed that Hamilton was 10.11 per cent too

high, yet the Court gave consideration to the test in adding to Black's estimate because it was too low, and used a figure slightly above that of Hamilton's although the test showed that Hamilton was approximately the same amount too high. The result of course, is impossible and the addition made by the Court, in our opinion, should not stand. The engineers made their estimates on the amount of rock excavation over the whole system. Any attempt to test the accuracy of these estimates by resurvey of but one small part of the line would, of course, produce a ridiculous result.

A further example of the fallacy of applying the percentage of rock excavation calculated on the resurvey or drilling test on a short line to the pipe line system as a whole may be shown by the following comparisons.

In Hamilton's valuation he estimated there were 35,760 cubic yards of shoot rock and 36,722 cubic yards of pick rock in the 125 mile line on which the resurvey or drilling test was made. (R. 434.) The resurvey on the Company's own figures showed 46,619 cubic yards of solid or shoot rock and only 169 cubic yards of pick rock. (R. 441.) If Hamilton's 577,428 cubic yards of pick rock and 256,861 cubic yards of shoot rock over the entire system are corrected in accordance with the percentages of shoot rock and pick rock developed by the resurvey, his 577,428 cubic yards of pick rock becomes 2,557 cubic yards and his 256,861 cubic yards of shoot rock becomes 468,189 cubic yards for the system as a whole, which means exactly nothing, and again shows the

fallacy of applying the result of the resurvey to the whole system.

As further proof of the absurdity of applying a percentage of increase based on the resurvey to Black's figures for rock excavation or a percentage decrease to Hamilton's figures as shown by the resurvey to other parts of the system, we cite the effect of this application on the Pampa-Wichita line, in which case the yardage of rock excavation is approximately the same, Black having 30,909 cubic yards as against Hamilton's 28,046 cubic yards of rock. Applying the same ratios obtained by the resurvey to the foregoing quantities of rock determined on the Pampa-Wichita line, Hamilton's rock quantities became 14,950 cubic yards and Black's quantities became 84,082 cubic yards. Applying the increase to Black's figures or the decrease to Hamilton's figures, obtains a ridiculous result.

There is no way in which the results of the resurvey could be applied to the system as a whole for the purpose of testing the amount of rock excavation without approaching absurdity.

We do not believe it is necessary to give further examples of the effect of attempting to use a percentage of increases or decreases based upon the resurvey. The Court, in attempting to use the result of the resurvey to increase Black's figure, reaches an impossible conclusion and so far as we are able to determine, any application which is made, obtains the same result. On some of the lines Black's estimate for rock excavation was lower than Hamilton's. On other lines Black's was higher

than that of Hamilton. Over the system as a whole, the estimates would level off to a fair average. The Commission so assumed in its findings and we believe that the Commission's findings were amply supported by the evidence. The Court disturbed the Commission's findings because of the resurvey of less than 3 per cent of the line. Having shown that the resurvey could serve no useful purpose in arriving at the amount of rock excavation, it is our opinion that the Commission's findings should stand, and that the Court was in error in adding $800,000 to the Commission's findings.

Assigned Error No. 12.

Engineering and Superintendence During Construction.

Both the engineers for the Company and the engineers for the Commission arrived at the value of engineering and superintendence by taking five percent of the physical properties, except certain items of general equipment consisting of Accounts Nos. 1316, 1380, 1381, 1382, 1383, 1384, 1385, 1387 and 1388, which would require no engineering. The Commission estimated engineering in the manner suggested and found the cost new to be $3,218,585, and the depreciated value to be $2,881,000.

The Commission used the depreciated figure. It is agreed by the parties that since no annual allowance was made for the depreciation of engineering and superintendence, that the account should not be depreciated. The Court, therefore, used the amount found by the Commission for the cost new, which increased the amount going

into the rate base $337,585. The Court added an additional $102,665 because it increased the value of the physical properties to which the percentage was applied. This, we contend is an error. This contention is based upon our argument that the Court was not justified in increasing the value of the physical properties over that found by the Commission. If the values of the physical properties found by the Commission are not increased, the cost new found by the Commission in the amount of $3,218,585 should be the value for Engineering and Superintendence.

Preliminary and Organization Expense.

The Commission found that preliminary and organization expense should be based on three-fourths of one per cent of the value of the physical properties, giving a cost new of $480,008 and the value was not depreciated.

The Court adopted the Commission's finding of three-fourths of one percent of the value of the physical properties, but added $20,617 because it increased the value of the physical properties. If our contention that the Court erroneously increased the value of the physical properties is correct, then the Commission's allowance in the amount of $480,008 is correct.

Administration and Legal Expenditure During Construction.

Both engineers estimated Legal and Administration Expense During Construction on the basis of one-half of one percent of the physical property. The Commission applied this figure to the values found by it and arrived

at a cost new of $340,094, and a depreciated value of $304,084. The Commission used the depreciated value in the rate base. The Court used the Commission's cost new. This was proper, because no annual allowance was allowed for depreciation. The difference between the value new and the depreciated value was $36,010, which the Court added to the Commission's value going into the rate base. The Court also added $10,256 because it increased the value of the physical properties. If our contention is correct that the Court was in error in increasing the value of the physical properties, then the addition of $10,256 is an error, and the Commission's value of the account new should be used.

Miscellaneous Construction Expenditure.

The Court allowed one percent of the physical value including engineering for miscellaneous and construction expenditures, and found the reasonable value to be $680,187 for the cost new and $608,169 as the depreciated value. Because of the agreement of the parties, the Court did not depreciate the account which added $72,018.00 to the Commission's rate base and added $20,513 additional because it increased the value of the physical properties. If our contention as to the value of the physical properties is correct, the Court was in error in adding $20,513 and the Commission's value of the account new should have been adopted by the Court.

Taxes During Construction.

The Court adopted the Commission's findings as to this account, but used the reproduction new value as found by the Commission instead of deducting depreciation. This was proper under the agreement between the parties.

Interest During Construction.

The Court adopted the Commission's allowance of six per cent for interest during construction, but added $468,652 because the Commission depreciated the item, and $120,000 because it increased the value of the properties. If our contention is correct as to the value of the physical properties, the addition of $120,000 was an error and the Commission's value new of $4,351,934 should have been adopted.

Although we have no argument with the Court's allowance of six percent for interest during construction, we do take issue with the Court's reason for allowing six percent instead of eight percent, and because its reason affected its allowance for going concern value, we believe that the matter should be discussed here. In its finding as to interest during construction, the Court said:

> "The Commission used a rate of six percent, the Company eight percent. It is customary to calculate this item at the present prevailing rate charged a person with good credit for temporary advances, which is now six percent. This throws upon the borrower, the owner of the property, the hazard of the borrowed money during the construction period, which must be considered. Two per cent is a reasonable allowance for that hazard, but it is customary

and preferable to make this allowance as a part of going concern value." (R. 308)

It would appear from the Court's opinion that it allowed 8 per cent for interest during construction, but chose to place 6 per cent under the heading, "Interest During Construction," and carried the other 2 per cent to going value. This, we believe was an error.

As stated by the Court, interest during construction is customarily calculated from the prevailing rate charged a person with good credit for temporary advances. The Court found this rate to be 6 per cent.

Under normal conditions, a greater rate of return on the value of the property when subsequently put into public service is allowed than for the use of money borrowed or advanced in construction, because the former involves the contingencies of operation and many other considerations, while the interest to be paid on money borrowed during construction is a fixed amount and is allowed in the rate base with no contingency attached to it. The interest during construction is a fixed allowance, while the earning of a rate after the business is in operation presents some hazard.

The appellee's contention as to the rate of interest to be allowed during construction was definitely set out in their reply brief before the Commission as follows:

> "If eight per cent is a proper rate of return for the investor to receive after the project is placed in operation, on what theory or by what process of reasoning can the conclusion be reached that this same investor is entitled to less return on his money during the period the plant is being constructed?

> You have the same investor and the same money going into the same project. Whatever is fair in one case must be fair in the other."

The Court appears to have adopted the same reasoning but allowed 6 per cent for interest during construction and carried the other 2 per cent over to going value.

The fallacy of this argument is clearly demonstrated by a quotation from the report of the special master in the Denver Tramway case, at pages 22 and 23 of his report:

> "It is common knowledge that a plant like this cannot be constructed in a short time. It follows that the present values contain an account for interest during construction. Under the evidence, it is my judgment that three years is a reasonable construction period in the present case, and that the interest should be computed for half of that time. I find 6 and ½ per cent per annum to be reasonable as the rate to be allowed. There is little relation to be found between a rate of interest to be allowed for the use of money borrowed or advanced in construction, and a rate of return on the value of the property when subsequently put into public service. The later involves the contingencies of operation and many other considerations."

The case is reported as Westinghouse, etc., v. Denver Tramway Co., 3 F. 2d., 235. The report is not included in the decision but it is approved. An examination of the decisions will disclose that interest during construction is never measured by the rate of return allowed. Even if it were, we believe 6 per cent would be reasonable under present conditions.

Going Concern Value.

Mr. Black included in the valuation, Going Concern Value in the amount of $3,820,000. Mr. Hamilton included it at $8,898,532.

The Commission found that both engineers had based their calculations largely upon idle plant following the period of construction, but before the line had reached the maximum capacity. The Commission further found that both witnesses had arrived at their calculations for idle plant upon a hypothetical basis without considering the actual facts in the case, and the actual experience of the Company. After considering the actual facts as to idle plant of the wholesale pipe line company as presented by the evidence in the case, and the actual experience of the Company, the Commission applied the tests which both engineers had laid down as to a proper measure of determining going concern value and found that $2,000,000 was the highest allowance justifiable under the evidence. The evidence from which the Commission reached its conclusion will be discussed later.

The Court appears not to have criticised the Commission's finding of evidence as to idle plant but considers two elements not presented by either of the engineers or the Commission, as follows:

6 per cent interest was allowed during the period of construction instead of 8 per cent, which the Court found to be a reasonable return after the property was put into operation.

The second element considered by the Court was an

annual allowance for depreciation during the construction period.

The Court summarized its reasons for adding the two factors to going concern value in its opinion as follows:

> "The period of construction was two years. Physical deterioration went on during that period when there were no earnings to offset it. The owner's money was embarked in a hazardous enterprise during the construction period; the Commission allowed only 6 per cent for interest during construction on the theory that an owner, with good credit, could borrow money at that rate. But the owner should be compensated for the risk involved in putting his credit back of the enterprise. If 8 per cent is a fair return on moneys embarked in this business, as we elsewhere find, that hazard was present during the construction period. The difference between 6 per cent interest during the construction period and an 8 per cent return in a business venture during construction, is $1,450,645, based on the Commission's valuation. During the construction period, there are no revenues, and depreciation and return (less interest during construction) must be capitalized in going concern value. After construction is completed, and some business is attached, there is an idle investment until the available business is fully attached, even under the most efficient management. ..."

While Mr. Black allowed depreciation and return on idle plant while the Company was acquiring its business, in the amount of $2,784,645, no similar allowance apparently was made during the construction period. The difference between 6 per cent interest allowed and 8 per cent return is $1,450,000. The parties agree on the Commission's figure of 2.96 per cent annual allowance for depreciation. Allowing half of that for the two year construction period, adds approximately $2,175,000. Without undertaking any

precise evaluation of this intangible asset, it is difficult to see how it can be fairly approximated at less than $5,000,000 which is about 6 per cent of the tangible values, a much lower percentage than the percentage customarily allowed." (R. 302, 310)

1.

Considering first the Court's finding that Going Value should be increased because it allowed but 6 per cent for interest during construction and the difference between 6 per cent interest allowed and an 8 per cent return is $1,450,645.

We desire to include here by reference, our discussion presented under the heading, Interest During Construction. For the purpose of brevity and to eliminate repetition, we will not reiterate here the argument there made as to why interest during construction should not be greater than 6 per cent and it should in no wise be measured by the rate of return allowed.

We do not believe that 6 per cent should be allowed for interest during the period of construction and because 8 per cent was not allowed for such item, an additional 2 per cent on the value of the properties should be added to Going Value. There is little relation between the rate of interest to be allowed during the period of construction and the rate of return. Even if it were conceded that the two rates should be the same, it is our contention that under present conditions an 8 per cent return is excessive and that a 6 per cent return would not be unreasonable nor confiscatory.

It should suffice to say that interest during construction

is customarily calculated on the prevailing rate charged a person with good credit, for temporary advances.

Rate of return involves the contingencies of operation and many other considerations, including competition and the possibility of earning the permitted rate over each annual period.

Interest to be paid on borrowed money during the construction period is a fixed amount, and is allowed in the rate base with no contingency attached to it. It is a part of the construction expense and just as definite as the expenditures made for physical properties.

We believe that the Court was in error in adding to Going Value because of the reason stated, and that the approval of the lower Court's theory would tend to increase the already difficult problem of valuing this intangible asset.

The Court speaks of the hazard of borrowed money to the borrower during the construction period and states as follows:

> "Two per cent is a reasonable allowance for that hazard, but it is customary and preferable to make this allowance as a part of Going Concern Value." (R. 308.)

We contend that the hazard of the business is not an element of Going Concern Value and we know of no decisions supporting the Court's statement.

Neither do we believe that the second element considered by the Court as a part of the Going Concern Value presents a sound reason for adding to the amount allowed by the Commission. The Court found that the

parties agreed on the Commission's figure of 2.96 per cent for annual allowance for depreciation and calculated that of such depreciation half for a two years construction period approximated $2,175,000, and considered it in arriving at its allowance for going value. (R. 311)

We believe that the Court was in error in allowing annual depreciation during the construction period. Annual allowance for depreciation is calculated on the service life of the property which begins when the property goes into operation. The construction period is not included in such life. The allowance is so calculated as to return the entire investment during the time the property is in operation. At the time the property goes into operation it is regarded as being in 100 per cent condition for the purpose of calculating the annual allowance and the rate of amortization is based on its estimated service life. This method was used in this valuation.

The result is that the Court's allowance for depreciation of 2.96 per cent during the construction period, is a duplication which again appears in the annual depreciation allowance.

It therefor appears that the Court overlooked this fact and erroneously gave consideration to annual allowance for depreciation during the construction period and added the same to going value on account of such oversight. We submit that any addition made for this element can not stand.

If the Court's theory upon which it added $3,000,000 to the Commission's finding as to Going Concern Value is erroneous, it only remains to be determined whether

or not the Commission's finding as to Going Concern Value was supported by the evidence.

2.

We recognize that it has been more or less the practice to add a certain per cent for Going Concern Value because this intangible item is difficult to ascertain by mathamatical calculation. The difficulty is not present in the case before us. The engineers broke down their elements of Going Value. The elements which they considered are those generally recognized as proper. The evidence showed, however, that they had made their estimates on hypothetical calculations and that a number of elements to which they gave consideration were not present in this case.

Mr. Black testified that he arrived at his value by allowing $15,000 for books and records, $1,020,000 for organization of the operating company, and $2,784,645 for interest and depreciation on idle plant; that is, on that part of the plant or plant capacity that would not be used after the plant was constructed, but before the capacity of the entire plant was used. It is therefore apparent that the largest part of Mr. Black's allowance for Going Concern Value consists of interest and depreciation on idle plant before the pipe line has reached its full capacity. (R. 444)

Mr. Hamilton testified that he had found his allowance for Going Concern Value by computing 10 per cent of the physical property value and calling the result Going Concern Value.

Mr. Hamilton testified that:

"I just took 10 per cent of the physical property value for this particular case for that item.

Q. You have not itemized it?

A. No, I have not itemized it in any way."

Mr. Hamilton testified further: (R. 446)

"Q. As I understand, then you did not arrive at it by finding the cost of attaching this business.

A. It is partially the cost of attaching the business, and the time of the engineers and others in negotiating the contracts, but that, for a wholesale situation, is a small item. The largest cost is the excess capacity that you will have to have for a period of three years, while your distributing companies are getting up to a point where they use the amount of gas that the size of the system is predicated on." (R. 448)

It is therefore apparent that Mr. Hamilton and Mr. Black considered idle plant while the line was reaching the maximum capacity as the largest element of cost to be considered in Going Concern Value.

Both witnesses testified that the Going Concern Value for a pipe line company would be less than the Going Value for a distributing plant. Mr. Hamilton testified to the difference between Going Value for a distributing plant and a pipe line company as follows:

"Q. Do you mean to say, Mr. Hamilton, that every plant of the same value should have the same allowance for going value?

A. No, because there would be a very different allowance between your pipe line plant or your distribution plant or an electric plant or something like that. There might be a wholly different basis.

Q. For instance you take the distribution plant, take the one here in Topeka, for example—
A. Yes, sir.

Q. If you assumed that you would reproduce it now, and it had no customers, it would mean you would have to attach in that case, thousands of customers before the business was established?
A. That is true, and 10 per cent allowance in that distribution plant would not be sufficient, in my judgment.

Q. Then take a pipe line company like this, and the number of customers you have is not very large, very many involved, don't exceed three or four hundred?
A. That is true.

Q. That should be taken into consideration in arriving at the Going Value in this case?
A. That is true." (R. 452-3)

It was therefore apparent and the Commission properly considered the main element of the cost of Going Value of this pipe line system, whose business is wholesaling gas, to be interest and depreciation on idle plant during the period the Company is acquiring its business and reaching its maximum capacity. The evidence in this case clearly disclosed that on the major part of the pipe line system there was very little idle plant following the construction period. The testimony on this matter is set out on pages 454 to 462 of the record as follows:

"Jarboe, superintendent of all pipe lines of the system, testified that the line to the Amarillo field was construeted for the purpose of taking care of

the present demand of the pipe line system. (R. 454)

Hamilton testified:

'Q. The line from Amarillo to Wichita, that as I understand, when it was built, was built for the purpose of taking care of the demand for gas you had at that time?

A. Yes, sir.' (R. 454)

"Mr. Eastman testified as to the Amarillo line from Texas to Wichita and Ottawa:

'Q. Now this line was built to Texas; was any addition to the market procured from that line, were any additional markets procured, any new customers? Are there any connected to that line between Texas and Wichita?

A. No new cities; there may be a few small towns along that line served, but they are inconsequential.'

'Q. Was there any other purpose than to supply existing markets?

A. No.' (R. 461)

"Eastman testified that the line from Ottawa to Kansas City was finished in 1929.

"In January, 1930, from the 16th to the 19th, the pipe line's capacity was exceeded and it was necessary to shut off the industrial gas in order to supply the demand for domestic gas. (R. 461)

"Hamilton testified the third line was built from Ottawa to Kansas City to take care of increased capacity there.

"Jarboe testified further that the lines to the Amarillo, Oklahoma City and Seminole fields are purely extensions to procure additional supply. No new customers were added: just went to take care of the market.

"At the time of the purchase of the Kansas Natural, the personnel was retained and continued. There was a demand for the gas line from Wichita to Texas, the Amarillo line. The same is true with reference to all the additions put on to the old system.

'Q. As I understand it each one of them was built because there was a need and it was necessary to complete this, to furnish gas to the main pipe line, or to places where it had already contracted or made arrangements to sell gas?

'A. One or the other.

'Q. That is correct?

'A. Yes.

'Q. Each one of those red lines denoting the construction of new pipe lines was built by the Cities Service in order to fill a need that existed at that time?

'A. Yes.

'Q. Upon their being completed they were then immediately put in use?

'A. Yes.

'Q. And have been in use and operation since then?

A. Yes.'" (R. 462)

It was therefore apparent, and the Commission so concluded, that both witnesses had arrived at their calculations for idle plant upon a hypothetical basis without considering the actual facts in the case and the actual experiences of the Company. *After considering the actual facts as to idle plant of this wholesale pipe line Company as testified to in this case and the actual experience of the Company, the Commission applied the tests which both engineers laid down as a proper meas-*

ure of determining going concern value and found that $2,000,000 was a proper allowance.

We believe that under this evidence $2,000,000 was the highest allowance which could, under any circumstances, properly be made for Going Concern Value. This allowance included an allowance for books and records, organization of the operating Company and a reasonable allowance for interest on idle plant. The Commission also considered the very apparent fact that a large number of the elements of Going Value were considered and included in other items of value by the engineers. (R. 137) This is made apparent by a reference to the overhead and intangible values calculated by the engineers and allowed by the Commission.

In considering the allowance for Going Value, we must take into consideration the general nature of the pipe line company's business as disclosed by the general testimony of the witnesses. In arriving at the reasonableness of the rate charged the pipe line company, we are considering the reproduction of the pipe line and not the distributing plants. The distributing plants were present and available before the pipe line was constructed. It was not necessary to construct the pipe line and then obtain a market. The market was present. The pipe line was constructed to supply an already existing market. (R. 461-2)

The distributing plants had been constructed for the distribution of artificial gas and natural gas which was produced from local fields. The local fields were being

exhausted. Artificial gas was not as practicable as natural gas. When the supply of natural gas was discovered, it remained only to construct the line from the supply to the already existing market. If the pipe line system were to go out of use and a new one be produced, the consumer and the distributing plants would be present and available.

The cost of attaching distributing companies to a pipe line system does not compare with the cost of acquiring and attaching customers to a distributing system. The burden of acquiring new customers is placed upon the distributing plants and not upon the pipe line company. The record discloses that the pipe line company serves but 120 some odd towns or distributing plants in the State of Kansas. The cost of attaching this already existing market would be negligible. (R. 448)

The regulation of extensive pipe line systems by a State Commission, is new. The extensive construction of inter-state pipe lines is of more or less recent origin. Rules for measuring Going Value of pipe line systems have not been laid down by the Courts. The Public Utilities Commission of Ohio recently had before it the question of the Going Value of a pipe line transmission system engaged in wholesaling gas in the case of the appeal of the Columbus Gas and Fuel Co., No. 5935. In the opinion, the Commission said:

> "It is quite manifest that the many reasons given by the experts as to why a going-concern value should be added to the physical value of the property within the city of Columbus does not obtain *as to the pro-*

duction and transmission system, as each of these was built for the definite purpose of supplying customers already secured and we feel that there is no justification for adding going-concern value to the production and transmission system. As we have before had occasion to state, if there was any definite cost to the company in doing those things which are so ingeniously developed as being the possible element of cost in the reproduction of the property, we would be inclined to allow them as a proper element of value, but we are not impressed with the fact that a going concern value amounting in the aggregate to millions of dollars can be built up on a theory that expenses are to be incurred after the property has been reproduced which were not, as a matter of fact, incurred in the original construction of the property. We cannot conceive that there would be any expense of attaching business to a producing pipe line company which has been built for the sole purpose of supplying already existing customers, nor are we impressed with the cost incident to training personnel, as the business of producing, transporting and distributing gas has been so long in operation that an abundant supply of well-trained personnel is always at the command of the company, and in these times there is probably a considerable oversupply." (P. U. R. 1933a P. 337.)

We therefore respectfully submit that the allowance of $2,000,000 made by the Commission was ample under the circumstances of this case.

Assigned Error No. 13.

GAS LEASES.

Summary of Argument.

All Leases, (1,262,361 acres).

COMPANY'S VALUATION (Fair Value)	$12,914,189.00
COMMISSION'S VALUATION (Fair Value)	6,279,237.00
COURT'S VALUATION (Book Value) (Finding 14)	5,727,272.00

Used and Useful, (71,267 acres)

COMPANY'S VALUATION	$ 5,124,940.00
COMMISSION'S VALUATION	2,874,390.00
DIFFERENCE between allowance by COURT for (ALL LEASES) and allowance by COMMISSION for 71,267 acres (USED AND USEFUL)	2,852,882.00

This account covers the value to be allowed for gas leases going into the rate base. The evidence pertaining to this account will be found on pages 462 to 508 of the record.

The account is not only important because of the addition which it makes to the valuation, but it also materially effects the operating income. The Company has asked for an annual allowance for reserve requirements pertaining to gas leases as follows:

> General Development Expense, including lease rentals, cost of acquiring leases and geological expense in the amount of $532,530.
>
> Amoratization of Non-Producing Leases, which is to provide a reserve to amoratize the cost of leases which are not producing, in the amount of $314,981.
>
> Dry Hole Expense, which is an annual allowance

to create a reserve to protect the Company against dry holes in prospecting its prospective acreage, in the amount of $174,747.

Depletion of Producing Leases in the amount of $70,509.

These annual allowances which the Company asks for its gas leases pertain to several hundred thousand prospective acres, a great part of which is not accessible to the system and is not even known to be capable of producing gas, and other proven leases including the Hugoton field, which is so far from the present pipe line that practically a complete new system would have to be constructed to make the acreage available to the present consumer. The Company asks to have the consumers pay in over a million dollars a year for the purpose of carrying its leases.

Two questions are presented pertaining to the value of this account.

(1). Was the Commission justified in excluding from the rate base, certain gas leases owned by the Company, on the ground that they were not "used and useful" and not likely to be within the near future?

(2). The valuation of the leases.

The Commission valued all of the gas acreage owned by the Company at $6,279,237, but included in the rate base as used and useful only 71,267 acres which it found from the reserves as testified to by the Company's engineers to be sufficient to supply the gas requirements of the Company for all of its produced gas for twenty-

two years. The Commission valued the 71,267 acres included by it in the rate base at $2,874,390.

The Company contended that the value of all of its gas leases is $12,914,189, and that the value of that part of its leases included in the rate base by the Commission is $5,124,940.

The lower Court included in the rate base, all of the Company's gas acreage, embracing developed, proven, probable and prospective acreage, and valued the same at $5,727,272, which was the book value. The lower Court disapproved the Commission's finding that only 71,267 acres of gas leases were used and useful in the system, and included all of the gas acreage. It stated its reasons in part, as follows:

> "Who shall determine what reserves are adequate? A Commission with no monies invested, or the owners of this pipe line which without gas is worse than useless? Within the limits of reason, undoubtedly that determination must be left with the owner."

The Court stated further:

> "The Commission's findings are predicated on a 20 per cent recovery; within two weeks of its order, the Texas R. R. Commission cut this to 4 per cent. What the future may hold by way of state action, no one knows."

As to the latter suggestion of the Court, it might be stated that the reason for the order of the Texas Commission was the fact that there was an over supply of gas in the field for which the independent operators could not find a market. A complete answer to the Court's suggestion however, is the fact that the Court has since

held the Texas order limiting the "take" to be invalid.

It is the contention of the Commission that the amount of reserves which a company should carry is best determined by its requirements.

A gas company should not be allowed to speculate in gas leases and have its speculations protected by charges to its consumers. Neither should it be allowed to place in its valuation for the purpose of increasing its return, gas reserves of an amount over and above those necessary properly to serve its customers.

The record in this case is quite complete as to the requirements of the pipe line company and there should be no difficulty in determining a reasonable allowance.

It is common knowledge that gas companies acquire leases for other purposes than those of simply supplying their consumers. One very common reason for acquiring leases is for speculation as to increase in value. When a company with a large acreage is able to acquire a monopoly by purchasing a large part of the available gas supply, the value of the acreage is necessarily increased and a profit to the company is the result. This is demonstrated in the present case by a sale to the Texoma Co., by the pipe line company now under consideration, in August, 1931, of 60,000 acres of leases. These leases cost the Company less than $15.00 per acre. Some of them it sold for $19.00 per acre and some at $45.00, netting the Company a profit of $1,110,157.61. The Company was protected against loss in this adventure by its annual requirements set up against its present consumers, but when the profit was made, the consumers received

no benefit by way of a credit to the operating income of the Company.

The lower Court gave little weight to this incident because it found that the gas leases which were sold were purchased by the pipe line company for sale to an affiliated company. This we believe to be contrary to the evidence. The record shows that a large part of this acreage was acquired by the pipe line company before the sale of the Texoma Co. was anticipated.

It is also true that gas acreage is acquired by gas pipe line companies over and above their actual reserve requirements, for the purpose of preventing competition. If they are able to obtain control of newly discovered gas acreage, in the territory which they are serving, they are of course able to prevent another company from coming in and making use of such gas for the purpose of competing with the existing system. This no doubt, is good business judgment on the part of the Company, but certainly the consumers should not be required to carry such burden. This is particularly true where the acquisition of the additional acreage has tended to cut off competition which might have supplied the consumers in the particular localities with their own local gas. Naturally, there can be no direct testimony that this was done. We believe, however, that the evidence submitted, when considered as a whole, raises a clear presumption from which such a finding can be made.

In this summary, we will not refer to the record in

setting out figures because such reference is made in the detailed discussion which follows:

The Company owns gas acreage which it classifies as follows:

Developed,	42,297 acres
Proven	196,170 acres
Probable	25,607 acres
Prospective	998,287 acres
Total	1,262,361

Of the proven acreage listed above, 123,440 acres is in the Hugoton field, located in Kansas and Oklahoma, all of which is 90 miles from the Company's present pipe line system and is therefore not available to the present system without a material addition to its system. The 998,287 prospective acres are not only distant from the pipe line but are not known to be capable of producing gas.

As to the material part of this acreage, there is no means by which the present market value can be ascertained. There are no purchasers for this large acreage because all the present companies have an over supply. Most of the acreage is already monopolized by large companies and if a purchase became necessary, the price could, to a great extent, be fixed by the present pipe line system. The evidence shows that the Burnett lease containing 63,880 acres which the Company owns in the Amarillo field, and is the largest producing field in the world today, cost the Company nothing except that it was to pay a minimum royalty on the gas pro-

duced of $50,000 per year. 21,158 additional acres in the proven Amarillo field cost $12.78 per acre which the Company now values at $93.00 per acre. The evidence further shows that there are 125 shut in wells in the Texas field owned by independent operators who are unable to sell their gas. This tends to show that there is very little practical value attached to a gas lease in the field unless it is in the hands of one of the few companies having a monopoly on the pipe line transportation.

The Company's sales reached the highest peak during the year 1930. During that year its daily average sales were 203,189 M. C. F. The requirements for the year were 74,163,945 M. C. F. During the year 1932 the Company's yearly requirements were 54,262,574 M. C. F., with a daily average of 149,548 M. C. F.

The evidence further showed that from its purchase contracts and producing wells, the Company had a potential open flow of 3,929,632 M. C. F., and that twenty per cent of this potential could be taken daily giving a daily supply of 785,926 M. C. F., which is more than 3½ times the average daily requirement.

The recoverable gas which could be taken from the Company's own gas leases (its gas reserve) and not including gas from its purchase contracts based on its engineer's estimate, is as follows:

Leases in Kansas, Oklahoma and Missouri, exclusive of the Hugoton field, 33,424,000 M. C. F., Hugoton field 688,590,000 M. C. F.; Amarillo field, 1,726,650,000 M.

C. F., totaling 2,448,664,000. This is available from the developed, proven and probable acreage in the amount of 233,582 acres and excludes the 998,287 prospective acres which is not taken into account in determining the reserve because it is not known that gas will be discovered and because they are better prospects for oil than gas, which is another reason for the Commission's belief that they should not be included in the rate base.

Based on the Company's experience for the year 1930, the year of its highest requirements, this gas reserve is sufficient to last the Company seventy-one years, for its requirements for produced gas. The Amarillo field alone, on the same basis, is sufficient for fifty years. It was on this evidence pertaining to the Company's requirements and its reserves that the Commission found but 71,267 acres to be used and useful in serving the present consumer.

The Commission found the following to be used and useful:

All developed acreage which included 22,090 acres in the Amarillo field; 20,207 acres in Kansas, Oklahoma and Missouri; all of the probable leases, except the Hugoton field, in Kansas, and Oklahoma in the amount of 1,060 acres; and undeveloped acreage in the Amarillo field in the amount of 27,910 acres. The Commission excluded the Hugoton field as not used and useful in the present system because it was undeveloped and too far removed from the pipe line.

Based upon the estimates of the Company's engineers

the recoverable gas (gas reserve) from the acreage allowed is 783,424,000 M. C. F., which, considered in connection with the Company's past experience, is sufficient to furnish the requirements for produced gas for over twenty-two years.

It was the opinion of the Commission that the testimoney of the officers of the Company as to the amount of reserve which the Company should carry, could not stand in the face of the actual facts as to its reserves and its requirements, and that there was no justification for including in the rate base, 998,287 acres of prospective leases which were not connected with the present pipe line system and may never be capable of producing gas, and the 123,440 acres in the Hugoton field which is undeveloped and is 90 miles from the pipe line. When this acreage is made available by development and reconstruction of the pipe line system, the additional investment made necessary and the additional earnings resulting from new customers reached can be given consideration. Those questions will present a pipe line system entirely foreign to the one we now have before us and will be met when they arise in the future. They can be given no consideration as to the valuation of the property that is used and useful in the present system.

A detailed discussion pertaining to the questions of the valuation of the gas leases follows.

GENERAL DESCRIPTION OF GAS LEASES.

The Company owned as of September 1, 1931, gas leases covering 1,262,361 acres of land situated in Kansas, Oklahoma, Missouri and Texas.

These leases grant to the lessee the right to drill for and take oil and gas and generally (with some exceptions) run for a period of ten years from date, after which, if oil or gas is not then being produced they expire, otherwise, they run so long as oil or gas is produced. The leases, in general, require the payment of rentals until development and require the lessee, after development, to pay to lessors a royalty of one-eighth of the oil and gas. The Company owns only the gas rights in these leases, the oil rights being held in most cases by affiliated companies.

These leases have been classified into developed, proven, probable and prospective.

"Developed" leases are those on which gas is actually being produced.

"Proven" are those adjacent to production, which will be drilled and on which it is considered gas will be found.

"Probable" consists of acreage adjacent to proven acreage having favorable geological structure, but which has not been completely tested.

"Prospective" consists of all other acreage. (R. 463)

The acreage owned by the Company, and its classification of its acreage is as follows:

COMPANY'S CLASSIFICATION.

	Developed	Proven	Probable	Prospective	Total A.
Texas	22,090	72,780	24,547		119,367
Hugoton (Kan. & Okla.)		123,440			123,440
Okla., Kan. & Mo.	20,207		1,060		21,267
Okla., Kan. & Texas				998,287	998,287
Totals	42,297	196,170	25,607	998,287	1,262,361

(Ex. 40) (R 463, 479, 489)

The Company does not produce from its own leases all of the gas it sells. Ever since its organization it has purchased the major portion of its gas. In 1930, the year of its greatest gas sales, it purchased about 54 per cent and produced 46 per cent. (R. 485)

In addition to the gas leases owned by the Company, it owns many gas purchase contracts which entitle it to the gas produced from leases in Kansas, Oklahoma and Missouri, covering 782,421 acres of land with 1,502 gas wells. (R. 485)

The gas wells situated on the lands covered by these purchase contracts, the gas from which the Company is entitled by paying the agreed price per M. C. F., have an open flow of gas of 2,138,170 M. C. F. per day. (R. 485)

Of the gas leases owned by the Company, only 42,297 acres have been drilled or developed, with 244 wells on the Kansas-Oklahoma developed acreage, and 60 wells on the Texas-Amarillo developed acreage. The Company thus owns but 304 wells. The remaining 1,220,064 acres of gas leases owned by the Company have not been drilled and are undeveloped. Nearly one million of these leases are prospective. 98 per cent of all of

the gas contained in the Company's gas leases (not including the purchase contracts) is in the Amarillo and Hugoton fields, and the remaining 2 per cent is in the Kansas and Oklahoma fields. (R. 489)

THE FAIR VALUE OF THE GAS LEASES.

We contend that in fact the leases owned by the Company have no market value and that it is no more possible to arrive at a market value of 1,262,361 acres of gas leases than it is to arrive at the market value of the entire plant of the Company. No purchaser could be found for this quantity of gas leases and they are valueless except in connection with a major pipe line system.

The value of these gas leases found by the Commission is in excess of their cost of acquisition and book value, and we submit should be sustained. The facts from which this valuation was found and the valuation found by the Commission and that claimed by the Company for the different classes of leases are as follows:

VALUE OF LEASES—AMARILLO FIELD.

(The valuations hereafter referred to are exclusive of all wells and equipment and cover the gas rights only.)

94,820 acres of the Company's proven gas leases are situated in what is known as the Amarillo (Texas)

PROVEN SWEET GAS AREA.

This "proven sweet gas area" is a portion of a huge field in the Panhandle and is approximaely 130 miles long and from 7 to 40 miles wide. It contains approxi-

mately 1,001,785 acres under all of which it is conceded that gas is present in large quantities.

Of the Company's acreage in this proven field 22,090 acres are developed, having 60 gas wells thereon. (R. 463, 489)

One of these leases is the Burnett lease. It covers 65,880 acres and requires a minimum payment of $50,000 per year in advance, for ten years, whether or not gas is taken from the lease. For the first two years, the royalty is one-eighth of 3½ cents per M; for the next five years, one-eighth of 4 cents per M; thereafter, one-eighth of 4 cents unless the price of gas at the well is increased, in which event the royalty is to be one-eighth of the weighted average price. The Burnett lease is not a solid block, there being within the block covered by said lease other gas leases owned by others than the Company, on which there are producing wells. Up to the present time the $50,000 annual payments required on this lease have exceeded the royalty earned on the gas taken. (R. 479)

Eight witnesses testified for the Company on the market value of its leases in the Amarillo field, five connected with gas companies, whose natural desire is to see that high valuations are placed on gas leases, and two employees.

Witnesses for Company place the market value of these leases at from $45.00 to $125.00 per acre, for the acreage situated within the "proven sweet gas area", with the higher value on the blocked acreage, and at from $5.00 to $25.00 for the probable. (R. 480, 481)

F. G. Holl, for the Commission, placed the value of the leases in the "proven sweet gas area" for 60,940 acres, blocked, at $45.00 per acre, for 33,767 acres, not blocked, at $25.00 per acre, and for the probable $1.00 per acre. (R. 481)

Holl's testimony showed that scattered acreage in Wheeler County, part of the proven sweet Amarillo field, where the largest wells in the entire field have been found, could be purchased at $5.00 per acre for both oil and gas; that in Potter County, near where the largest wells have been brought in, in September, 1931, a lease which was about to expire consisting of 5,000 acres, was renewed at $8.00 per acre. (R. 480)

The Company's evidence showed that in August, 1931, it conveyed to the Taxoma approximately 60,000 acres of leases with nine producing wells, comparable with the acreage retained in the proven sweet area, some at $19.00 and some at $45.00 per acre, which cost the Company less than $15.00 per acre, and that on this sale the Company made a profit of $1.110,157.61, not including a bonus of $121,000 paid from the proceeds of said sale to the Empire Gas & Fuel Company, an affiliated Company. (R. 480)

In addition, the Company at the same time sold to the Texoma nine gas wells at $216,000, which cost the Company only $205,000 at a profit of $11,000. The evidence shows that some of the leases which were transferred to the Texoma, August, 1931, were procured by the Company as early as 1928, and as the agreement to transfer leases to the Texoma was not made until 1930

it cannot be, as claimed by the Company, that these leases were all purchased for the Texoma, because many of them were acquired by the Company long before any deal with the Texoma was effected. (R. 492)

The books of the Company show that from January 1, 1930, to June 30, 1931, it purchased 21,158 acres in the proven sweet Amarillo field, now valued by it at $93.00 per acre, at an average cost of $12.78 per acre. (R. 480)

The evidence shows a large oversupply of gas developed by gas companies in the Amarillo field which cannot be sold for lack of market.

Gas was being sold in this field at 2 cents per M.C.F. at the well in September, 1931. (R. 481)

That in September, 1931, there were 125 "shut-in wells" with an open flow of 2,260,000,000 c.f. per day, with no outlet or market. (R. 481)

That the Lone Star Gas Company Pipe Line was connected to 65 wells in this field, and for the first six months of 1931, it took from these wells only 100 M.C.F. per day, at the rate of $2.00 per day (less than interest on cost of well), and that operators were not drilling on account of an over supply. (R. 481)

Practically all of the lands in the Amarillo proven sweet field have been leased by the eleven major pipe-line companies, which have pipe lines into this field, and by certain independent operators who own the "shut-in" wells. These gas companies have the monopoly of these leases and there is no market for gas in this field except as made by regulated demand for gas. Due to this fact

it cannot be said that gas leases in this field have any market value, fair or otherwise. (R. 481)

PROBABLE ACREAGE—AMARILLO FIELD.

The Company owns 24,547 acres of gas leases in Texas situated outside of the "proven sweet gas area" classed by it as "probable," some of which are in the sour gas area, and therefore not adapted for gas for domestic use. (R. 481, 492)

The testimony of the witnesses for the Company as to the value of this acreage varied. Some stated that part of these are worthless, others at from $5.00 to $25.00 per acre. (R. 481)

F. G. Holl, for the Commission, placed the fair value of the gas rights in that part of this acreage, which he classed as "favorable," at $1.00 per acre, and 50 cents per acre for that part which he classes as "prospective," and nothing for the remainder of the Texas acreage. (Ex. 46) (R. 481)

The Commission valued this probable acreage at not more than $2.00 per acre, and found that the value of these 24,547 acres of probable leases was not more than $49,094 and we submit that this is a fair valuation.

The Company values its acreage in the Amarillo field at—

94,920 acres proven	@	$93.64	$8,879,628
24,547 acres probable	@	$17.20	422,367
Total			$9,301,995

The Commission found the value of the gas leases in the Amarillo field to be not in excess of:

Proven 60,940 acres, blocked	@ $50.00	$3,047,000	
Proven 33,880 acres, not blocked	@ 35.00	1,185,800	
Probable 24,547 acres	@ 2.00	49,094	
Total			$4,281,894
Difference			$5,020,101

(R. 464, 478)

We submit that said acreage has in fact no market value, because in August, 1931, the Company sold approximately 60,000 acres of gas leases from this field comparable with those retained in this field, some at $19.00 and some at $45.00 per acre, which had cost the Company but $15.00 per acre, and because from January 1, 1930, to June 30, 1931, the Company purchased 21,158 acres of these leases at an average cost of $12.78 per acre, that the valuation placed on these leases by the Commisssion is fair and indeed liberal.

VALUE HUGOTON LEASES.

(Kansas and Oklahoma.)

The Company owns 123,440 acres of gas leases in the Hugoton field situated in Northwestern Oklahoma and southwestern Kansas, all of which it contends are "proven." (Ex. 40)

This is another enormous gas field estimated to comprise 1,000,000 acres of gas-productive lands. Its limits

are not yet defined. They can be determined only by additional drilling. Dr. Raymond C. Moore, state geologist, estimates the gas reserves in this field as sufficient to supply all of the State of Kansas, on the basis of the amount of gas now used in Kansas, for a period of over 100 years. There is a market for but a small portion of the developed gas in this field. Little drilling has been done, but there is sufficient drilling to demonstrate that this is a rich field of gigantic proportions. (R. 482)

Of the Company's acreage, F. G. Holl, for the Commission, classified 84,367 acres as "proven," 32,008 acres as "probable," and the remainder as "prospective." (R. 463)

There is no development and no wells on any of the Companys acreage in the Hugoton field. The Company's leases consist of one large lease, the Stonebreaker lease, covering 25,280 acres, and over 500 smaller leases. The terms of each of these 500 leases require the drilling of a well within ten years from its date; otherwise the lease expires at the end of ten years. The cost of a well in this field is over $20,000.00 and if the company is to hold these leases it will have to drill at least 500 wells within seven years from this date, that is, before 1940, at a cost of over $10,000,000.00 or said leases undrilled will expire. The Company has no pipe line within ninety miles of these leases. (R. 482)

Witnesses for Company, four in number, testified that the fair market value of the gas rights in these leases, which are in the proven area, is from $3.00 to $10.00 per acre, and the Company claim that the fair market value

of its 123,440 acres of leases is $1,172,680.00. (R. 482)

Against this is the testimony of F. G. Holl that at the time of the hearing, leases conveying both the oil and gas rights could be purchased in the proven area of this field at $1.00 to $2.00 per acre; that the Derby Oil Company had within sixty to seventy days prior to his testimony purchased both the oil and gas rights on 5,947 acres of leases, all in this proven area, at $1.00 and $2.00 per acre. (R. 482, 483)

Holl valued the gas rights in these leases at $7.50 per acre for the proven blocked, $1.50 for the proven unblocked, $1.00 for the probable, and 50c for the prospective, total $313,771.00. (R. 483)

The Company values this acreage at $1,172,680 or $9.50 per acre.

The Commission valued it at $556,116.00, at $7.50 for the blocked proven area; $5.00 for the unblocked proven, $2.00 for the probable area. The difference is $616,564.00. (R. 483)

The cost of these leases to the Company was from $1.50 to $6.00 per acre.

As the undisputed evidence shows that at the time of the hearing the Derby Oil Company purchased 5,947 acres in the proven area at $1.00 per acre, we submit that the valuation found by the Commission is liberal.

VALUATION KANSAS-OKLAHOMA LEASES.

(Exclusive of Hugoton.)

The following is a classification, acreage and valuation by the Company of its leases in Kansas and Oklahoma, where the Company owns 21,267 acres of gas leases: (Tr. 717-719)

Proven and Developed:				
Kansas	16,125		$138,240	
Oklahoma	4,082		239,700	
Totals		20,207		$ 377,940
Probable Acreage:				
Kansas	80		8,000	
Oklahoma	980		57,000	
Totals		1,060		65,000
Totals		21,267		442,940

(Tr. 935)
(R. 483)

This classification and valuation was accepted by the Commission and is not in dispute.

VALUE OF PROSPECTIVE ACREAGE.

The amount of the prospective acreage is 998,287 acres. It is scattered throughout Texas, Oklahoma, Kansas and Missouri. From its location its value, if any, is for oil and not for gas.

The leases were taken in most instances by affiliated companies for oil and gas, and the gas rights then assigned to the Company. An inspection of the map attached to the Company's exhibit 3, Davis report, wherein the amount of acreage held by the Company is written on each county, will show that the most of this prospec-

tive acreage is not accessible to the pipe lines of the Company.

These leases are not considered in arriving at the gas reserve of the Company on account of their speculative character.

This prospective acreage is what is commonly designated as "wild-cat" leases.

From July 1, 1931, to November 1, 1931, the Company surrendered 61,471 acres as not of sufficient value to warrant payment of rentals. (R. 493)

Mr. Nesbit, the Company's chief geologist, valued this prospective acreage at $2.00 per acre. (R. —)

Ralph E. Davis, geologist and gas engineer, the Company's witness, classified 1,031,127 acres of the Company's acreage as "prospective" and placed its value at $1.00 per acre. (R. 492)

Holl, for the Commission, classified 268,909 acres as favorable at $1.00 per acre, 616,073 acres as prospective at fifty cents, and the remainder as of no value for gas. (R. 493)

The company values these leases at $2.00 per acre, the Commission found that the value of this prospective acreage to be not in excess of $1.00 per acre. Company's value, $1,996,574; Commission, $998,287; difference $998,287. (R. 464, 478)

SUMMARY.

The value of all of these leases, as claimed by the Company, is $12,914,189.00 as follows:

Company's Classification and Valuation of Acreage.

Name of Field	Acres Proven	Acres Probable	Acres Prospective	Total Value	Value Per Acre
Amarillo	94,820			$8,870,628	93.54
do		24,547		422,367	17.20
Hugoton	123,440			1,172,680	9.50
Kansas & Okla. (All other)	20,207			377,940	18.70
do		1,060		65,000	61.32
do			998,287	1,996,574	2.00
Totals	238,467	25,607	998,287	12,914,189	
Grand Total		1,262,361 acres. (R. 464)			

The valuation of all of the Company's leases as found by the Commission is not more than $6,279,237.00 as follows:

Commission's Classification and Valuation of Acreage

	Acres		Value per Acre	Fair Market Value
AMARILLO FIELD (Texas)*				
Developed and Proven				
Blocked	60,940	@	$50.00	$3,047,000.00
Not blocked	33,980	@	35.00	1,189,300.00
Total	94,920*			$4,236,300.00
Probable Acreage	24,547	@	2.00	49,094.00
Total	119,367			$4,285,394.00

*Of the above 22,690 acres are developed with sixty producing wells

HUGOTON FIELD (Kansas and Oklahoma)				
Blocked	25,280	@	7.50	189,600.00
Not blocked	59,087	@	5.00	295,435.00
Probable	32,008	@	2.00	64,016.00
Total	116,375			
Prospective	7,065	@	1.00	7,065.00
Total	123,440			$556,116.00

	Acres	Value
Proven: Kansas, Oklahoma and Missouri	20,207*	$377,940.00
Probable: Kansas, Oklahoma and Missouri	1,069	35,000.00
		$412,940.00
Prospective	968,287@$1	968,287.00
Grand Total	1,262,261	$6,279,227.00

*These are developed with 244 wells.

The difference is $6,634,952.00

(R. 478)

GAS REQUIREMENTS.

The Company's gas requirement for all of its consumers, domestic and industrial, for the year of 1930, that being the year of its highest sales, was 74,163,945 M c. f., or an average of 203,189 M c. f. per day. This is calculated on an 8-Oz base. As the gas which it produces and purchases is on a 2-lb. base, the above amount should be reduced 9.2 per cent. However, in the calculations appearing hereafter the reduction is not made in order to compensate for the gas used in the Company's stations and for leakage which the company states is 5 per cent, so that this 9.2 per cent is more than sufficient to absorb this loss. (R. 485)

In the year ending June 30, 1932, and on the same 2-oz. base, the company's requirements for all its consumers was 54,621,574 M c. f., or a daily average of 149,648 M c. f. (R. 484)

For the year of 1930, the Company produced from its own wells 34,401,978 M c. f. and purchased 39,761,967 M c. f. In other words, it produced 46 per cent and purchased 54 per cent of its gas requirements. The amount of gas produced by the Company in the year, 1930, is the largest amount the Company has ever produced from its own wells, either before or since that time. The remainder of the gas sold is purchased from others. (R. 491)

In addition to the gas leases owned by the Company, it owns through purchase contracts the right to the gas produced upon 782,421 acres in Kansas and Oklahoma,

adjacent to and connected to its pipe lines, on which there are 1,502 wells.

The open flow of gas from these purchase contract wells (potential) is 2,138,170 M c. f. (R. 485)

The gas from these purchase contracts, together with gas from the Kansas and Oklahoma wells is sufficient to furnish the entire requirements of the Company with the Amarillo field and pipe line cut off, and in fact has done so when the Amarillo line has been shut down. (R. 494)

It is proper to take from a gas well at least 20 per cent of its open flow; Nesbit, 20 per cent; Davis, 20-30 per cent; Hardy 25 per cent. (R. 485)

At the time of the peak demand, January 16, 1930, the purchase contract wells actually put into the pipe line 12 per cent of their open flow. The reason why a greater proportion was not taken was due to lack of capacity of the pipe line to carry the gas. (R. 493)

The open flow per day (potential) of the wells owned by the Company, as of July 1, 1931, was 60 wells, Amarillo, 1,532,625 M. c. f. Kansas, Oklahoma and Missouri 244 wells, 258,837 M c. f. so that the total open flow (potential) of all the wells controlled by the Company was:

	M c. f.
Purchase contract	2,138,170
Amarillo—(60 wells)	1,532,625
Kansas, Oklahoma & Missouri (244) wells	258,837
Total open flow (potential)	3,929,632

(R. 485)

The highest demand, on the coldest day (peak load), occurred on January 16, 1930. At that time the Company used 330,000 M. c. f. which was the full capacity of the company's pipe line system. The maximum capacity of the Amarillo pipe line, a 20 inch line, is 125,000 M. C. F. per day. (R. 485, 500)

On the basis that 20 per cent of the open flow of the produced and purchased gas is available for use, the company had daily available 20 per cent of 3,929,632 M. c. f. or 785,926 M. c. f., which is more than three and one-half times its daily average requirement, for the year when it sold the largest amount of gas and five times its daily requirements for the year ending June 30, 1932, and is two and one-fourth times the peak load and maximum capacity of its pipe-line system.

It is claimed that the company cannot put into its pipe lines 20 per cent of the open flow in the winter months, when the line pressure is high. If this be true, it does not prove the gas is not there or available. It only shows that the Company's pipe line and compressor capacity is insufficient. (R. 493)

Mr. Stuntz, for the Company, testified:

"Q. Now what percent of open-flow gas can you get out of the Oklahoma City wells?

A. About 10 per cent of the dry gas in Oklahoma City would be about all the line would carry.

Q. You mean on account of the size of the line?

A. Yes."

* * * * *

"Q. Let me see if I understand you, then. Is it true that the capacity of your pipe line at Oklahoma

City is such, or has been less than the capacity to obtain gas in purchase contracts?

A. That is right.

Q. The gas is there, but your line is not sufficient to carry it?

A. That is right."

It has been demonstrated by actual experience that 12 per cent of the open flow of the purchase contract wells can be delivered into the pipe lines in the winter when the line pressure is highest, and this means that the daily amount of gas available to the company with its present set up, is at least 12 per cent of 3,929,532 M. c. f. or 471,555 M. c. f. per day, which is over 70 per cent more than the capacity of its pipe-line system and highest demand it has ever experienced.

This 12 per cent of the open flow is more than double its average daily requirement for the year, when that requirement was greatest, and more than three times its average daily requirement for the year, ending June 30, 1931.

The open flow of the 60 wells of the Company in the Amarillo field, as of July 1, 1931, was 1,532,625 M. c. f. of gas. The maximum capacity of its 20-inch Amarillo pipe line is but 125,000 M. c. f. per day. It will be seen that the company in the Amarillo field has available, based on a 12 per cent take, 58,000 M. c. f. in excess of the capacity of its Amarillo pipe line, and based on a 20 per cent take, more than double the amount of gas that it has facilities to transport from this field.

The Company in its argument in the lower court laid great stress on the fact that after the hearing before the Commission, the Railroad Commission of Texas had made an order limiting the take of gas from the Amarillo field to 4 per cent of the open flow, in an effort to provide a market for the "shut-in" gas in this field. This order never became effective for the Company promptly procured a restraining order against its enforcement and on final hearing before a three-judge court, it was declared unconstitutional (Cities Service Gas Co. v. Terrell, 2 Fed. Supp. 168).

What has there been said as to gas requirements applies only to the sufficiency of developed gas for the company's daily requirements and has no reference to its gas reserves on which it must rely for its future supply.

GAS RESERVES.

By gas reserves is meant the gas actually recoverable from the proven and probable leases. In determining the gas reserves of the Company, the 998,287 acres of prospective leases are not taken into account because of their speculative character.

The Company introduced Exhibit 3, being report by Ralph E. Davis a gas engineer and geologist of national repute, who had been employed by the Company to make an exhaustive survey and to testify as to its gas holdings and gas reserves. This report is bound, contains 98 pages and 14 tables and a map showing its pipe-line system, location of its gas fields, and the gas

acreage held by the company in each county in Texas, Oklahoma and Kansas. It covers, among other things, a list of all of its wells, together with the date when drilled, their initial rock pressure and volume, their rock pressure and volume as of July 1, 1931, their depth, the amount of gas reserve remaining, the amount of gas produced and sold by the company from 1927 to date, a list of its gas purchase contracts, and the open flow of gas from the wells covered by said contracts, and a classification of all of the Company's leases into developed, proven, probable and prospective, and numerous other data, including a statement of the recoverable gas reserves covered by the gas acreage held by the Company, except as to the prospective acreage.

Mr. Davis is the same witness who testified for United Gas and Fuel Company in the case of United Gas & Fuel Company v. Public Service Commission of West Virginia, 278 U. S. P. 322.

A statement of the acreage, classification and the recoverable gas reserve of the Company which is not disputed was introduced by the Company in this Exhibit and is as follows:

RECOVERABLE GAS FROM ALL PROVEN AND PROBABLE ACREAGE AND CLASSIFICATION.

	Estimated Gas Reserves M c. f.	Acreage
Kansas-Oklahoma (except Hugoton and Mo.		
Proven, developed	23,858,000	19,882
Probable	9,566,000	1,020
Total	33,424,000	20,902
Hugoton Field:		
Proven	492,100,000	49,210
Probable	196,490,000	28,070
Total	688,590,000	77,280
Amarillo field:		
Proven:		
Developed	585,600,000	39,040
Undeveloped	836,700,000	55,780
Total	1,422,300,000	94,820
Probable	304,350,000	40,580
Total	1,726,650,000	135,400
Grand total	2,448,664,000	233,582

(R. 486, 487)

It will thus be seen the Company's total recoverable gas reserve from 233,582 acres of proven and probable acreage, including that acreage in Kansas, Oklahoma and Missouri, 20,902 acres; the Amarillo field, 135,400 acres; Hugoton field, 77,280 acres; is 2,448,664,000 M. c. f. of gas and that 98 per cent of this recoverable gas is in the Amarillo and Hugoton fields, of which in excess of 70 per cent is in the Amarillo field.

That part of the Amarillo field known as the proven Sweet gas area is 130 miles long, from seven to forty miles wide, containing approximately 1,001,785 acres, all of which is proven and in which no dry hole has been encountered. Wells come in in this field producing from 6,000,000 to 170,000,000 cu. ft. of gas per day. It is the most gigantic and most prolific gas field ever discovered.

Davis testified that the gas-producing sand over the entire proven Sweet is 70 feet thick on the average, and that the recoverable gas, that is, the amount of gas which can be taken out after leaving 20 per cent of the gas in the ground, is 15,000,000 cu. ft. per acre, and stated that this estimate is low and that it is possible that from one and one-half to two times this recovery of 15,000,000 cu. ft. of gas per acre will be obtained. (R. 486)

Davis testified that although some of the wells of the Company in Carson County had been producing into its pipe line for three and one-half years, the average rock pressure on July 1, 1931, had diminished only 6 lbs., from 412 lbs. to 406. (R. 492)

Based on the assumption that the company annually will be required to produce from its owned gas leases as much as it produced from them in 1930, to-wit: 34,401,978 M. c. f., the year when it produced and sold its largest amount of gas, its gas reserve in the proven and probable acreage, excluding the prospective, will last for over seventy-one years.

Its proven and probable acreage in the Amarillo field alone is sufficient for fifty years.

Or if the Company should cancel all of its purchase contracts and take all its gas requirements, which for 1930 was 74,163,945 M. c. f., including gas purchased, from its gas reserves its gas reserves would last for thirty-three years.

We believe that from the foregoing it is evident that the Company owns many more gas leases than are "used and useful" and devoted to the use of supplying gas to its customers. It is a fair inference from the facts in evidence that the Company acquired these excess leases expecting to sell them at an enhanced price. The evidence shows that it did sell 59,788 acres of gas leases to the Texoma in 1931, at a profit of more than $1,000,000.00. (R. 480)

GAS LEASES USED AND USEFUL.

It has been said:

> "The well-established rule of law is unquestioned, that what the company is entitled to demand in order that it may have just compensation, is a fair return upon the reasonable value of the property at the time it is being used for the public." (Pond on Public Utilities, Sec. 591; San Diego Land & Town Co. vs. National City, 174 U. S. 757; 43 L. Ed. 1154)

We believe this is a correct statement of the law and that the mere fact that the officers of the company have testified that they consider all of the 1,262,361 acres of gas rights owned by the Company as a necessary and a prudent purchase, is not conclusive that all of these

gas leases are presently used and devoted to the public use, if the physical facts show, as we contend they do here, that all of these gas rights are not now used, and that the present rate payers do not and will not in the near future receive any benefit from most of them.

This is not saying that the officers are to be criticized for purchasing these leases, nor is it contended that if the time ever comes when said gas rights are in fact devoted to the public use, they should not then be included in the rate base on which to earn a return.

As was said by Rose, C. J., in United Gas and Fuel Company v. Public Service Commission of W. Virginia, 14 Fed. (2d) 221:

> "At the risk of tiresome repetition we can say that we do not criticize plaintiff for acquiring any or all its gas rights. It was doubtless wise to get them. All that we decide is, that, in arriving at the rate base upon which plaintiff is entitled to a fair return, we may not combine two opposing theories. We are not justified in saying that, because plaintiff's investments in gas reserves were prudent, its reserves immediately went into use, and that therefore plaintiff is entitled to have them appraised at the many times higher value it says they now have."

The Commission found that of the Company's acreage, only the following was used and devoted to public use: 50,000 acres in the proven sweet gas Amarillo Field, of which 45,830 acres are blocked and 4,170 acres are not blocked. In addition, all of the developed and probable acreage in Kansas, Oklahoma and Missouri (except the Hugoton field) 21,267 acres, total 71,267 acres, valued

by the Commission at $2,874,390.00, and included this value in the rate base and excluded the value of the remaining acreage. (R. 150)

In this 71,267 acres, found to be "used and useful" are included:

(1) All of the Company's developed acreage, wheresoever situated; Amarillo, 22,090 acres, with 60 wells; Kansas, Oklahoma and Missouri, 20,207 acres, with 244 wells.

(2) 27,910 acres proven, undeveloped acreage in the Amarillo proven sweet gas area.

(3) All of the probable acreage in Kansas, Oklahoma and Missouri, 1060 acres (except Hugoton field).

That is, this 71,267 acres comprises 50,000 acres proven in the Amarillo field with all the wells in that field, and 21,267 acres, all of the developed, proven and probable acreage in Kansas and Oklahoma, (except Hugoton), containing all the wells owned by the Company wherever situated.

The recoverable gas reserve in this 71,267 acres, according to the testimony offered by the Company is:

	M c. f.
50,000 acres—Amarillo	750,000,000
21,267 acres, Kansas, Oklahoma and Missouri	33,424,000
71,267 acres	783,424,000

(R. 486) which is sufficient to furnish all of the Company's requirements, excluding the gas purchased under

its purchase contracts, on the basis of its requirements for the year, 1930, for twenty-two years, plus.

$$\frac{783,424,000 \text{ M c. f.}}{34,401,978} = 22 \text{ plus}$$

The Commission has thus excluded from the rate base the following:

	Proven	Probable	Prospective.
Amarillo field	44,820	24,547	.....
Hugoton (Kansas and Oklahoma) (Company's Classification)	123,440	.....	.....
Prospective—all	.....	.....	998,287
Total	168,260	24,547	998,287
Grand Total			1,191,094 acres

All of this excluded acreage is undeveloped.

The acreage in the Hugoton field excluded comprises 123,440 acres, classified by the Company as all proven; classified by the Company's expert, Davis, as 49,210 acres proven, 28,070 acres probable; by Holl, for the Commission as 84,367 acres proven, 32,008 acres probable, and 7,065 acres prospective.

None of the company's acreage in this field is drilled, and all of it is distant at least ninety miles from any pipe line owned by the company. It is held by the company through leases which run for ten years with now about seven years to run. These leases require that an annual rental be paid and that a well be drilled within

the term of the lease, or it will expire. The number of these leases is in excess of 500.

The cost of drilling and equiping a well in this field is not less than $20,000, and if the Company is to hold these leases, it must drill within the next seven years over 500 wells at a cost of over $10,000,000, and in addition pay an annual rental in a substantial amount.

The prospective acreage excluded amounts to 998,287 acres, and has already been described. As stated, it is "wild-cat" territory. Its value, if any, is for oil and not gas, is scattered, and very little of it is available to the company's pipe line. It was not included in estimating the gas reserve.

In the allotment of 71,267 acres of leases as "used and useful", there are 28,970 acres of land in the proven sweet area of the Amarillo field, which are not developed, and 1,060 acres in Kansas, Oklahoma and Missouri which are probable and undeveloped, making a total of 29,295 acres in the acreage assigned as "used and useful", which the company may in the future develop as that becomes necessary.

It will thus be seen that by the allotment of the 71,267 acres to the company as presently "used and useful" there has been included all of the Company's developed gas acreage and wells wherever situated; all of its proven and probable acreage in Kansas, Oklahoma and Missouri, (except Hugoton), with a recoverable gas reserve of 783,424,000 M. c. f. as follows:

SUMMARY OF GAS LEASES—USED AND USEFUL.

DEVELOPED.	Acre	Wells	Recoverable Gas M. c. f.
Amarillo	22,090	60	331,350,000
Kansas, Oklahoma & Missouri	20,267	244	33,858,000
PROVEN UNDEVELOPED			
Amarillo	27,910	None	418,650,000
PROBABLE			
Kansas and Oklahoma	1,060	None	9,566,000
	71,267	304	783,424,000 M. C. F.

with sufficient reserves of recoverable gas to last (on the basis of its requirements for produced gas in 1930) for over twenty-two (22) years. In addition to this reserve, the Company owns purchase contracts entitling it to the gas from 782,421 acres in Kansas and Oklahoma, having 1,502 wells and a daily open flow of 2,138,170 M. c. f.

To us it seems unjust to require the present gas consumer to pay a rate for gas based on a return on the valuation of leases which are not used for them, and which if ever used will not be until the distant future. To do so would permit the utility to speculate in leases at the expense of the consumer, for it is the practice of the company to charge as an expense the cost of leases which prove worthless, and the expense of dry holes, but when the lease proves valuable, to add the increased value over its cost, to the rate base, and where the leases are sold at a profit, not to include the profit in its earnings, as

was the case in the sale of leases and wells to Texoma where the Company realized a profit of over one million dollars.

The gas situation has undergone a complete change within the last five years. The Amarillo and Hugoton fields have been developed within that time. Prior to that time the problem was how and where to get gas, and utilities based their rates on the agreed presumption that the gas supply would be exhausted in from seven to ten years, and asked to amortize their entire property within that time.

Now the problem is to find a market for surplus gas.

Doctor Raymond C. Moore, State Geologist, of Kansas testified that the recoverable gas in the Hugoton field alone is sufficient to supply all of the requirements of Kansas, domestic and industrial, at the present rate of consumption, for over one hundred years.

Since the hearing before the Commission, the Burton field—about twenty-one miles from Wichita and eleven miles from Hutchinson, Kansas, has been discovered. Its limits have not yet been defined. At the time of the hearing in the lower court it had wells with an open-flow capacity of 270,000,00 cu. ft. per day, with a rock pressure of 1,200 lbs. Since that time the field has been greatly extended. The Company has a pipe line within three miles of this field which is connected to two of the wells in this field. (R. 489)

The problem confronting the Texas railroad Commission in the Amarillo field is how to conserve from waste and to provide a market for the vast amount of "shut-in"

gas, that is, gas wells which have been drilled by independent operators which are shut in for lack of market.

The first attempt to provide a market for this "shut-in" gas was by the common purchaser act, which required the gas companies to purchase pro rata this gas. When that was declared unconstitutional, (Texoma Natural Gas Co., v. Railroad Commission, 59 Fed. (2nd), 750) the Texas Commission made its recent order referred to by the Company in the lower court, limiting the "take" to 4 per cent of the potential (open flow).

The object of this order was to provide a market for this "shut-in" gas. Since the decision of the lower court, this order has been declared unconstitutional (Cities Service Company v. Terrell, 2 Fed. Supp. 168, supra), and the take now is only limited to 25 per cent of the open flow.

The action of the Commission in including in the rate base only that acreage which presently and in the near future will be "used and useful" is in accordance to the established practice and is supported by the authorities.

AUTHORITIES.

In the case of Spring Valley Water Co. v. San Francisco, 165 Fed. 667, decided October 7, 1908, District Judge Farrington said (at page 697):

> "It is not just to compel consumers to pay for more than they receive, or to pay complainant an income on property which is not actually being used in gathering and furnishing water. If in this case the company, in anticipation of the growth of the

> city and its future needs, acquired property for future use at a cost of hundreds of thousands of dollars which is now worth millions, it has acted wisely, but it should be satisfied with the goodness of its bargain and the enhanced value of its property without asking in addition gratutities from its customers in the way of higher rates. When the property does come into necessary service, the company is entitled to have it credited at its then fair and reasonable value for rate-fixing purposes."

In Acquackanonk Water Company v. Board of Public Utility Commissioners, 100 N. J. L. 169, Affirming 1. N. J. Mis. R. 575, 125 Atl. 33, P.U.R. 1924 E, 436, decided May 19, 1924, the New Jersey Court of Errors and Appeals affirmed a judgment of the Supreme Court which had affirmed the Commission's order. On the matter of unused property the court said (at page 438, P. U. R.):

> "The first point made by the water companies is that the Board erroneously reduced the value of the property by excluding one-half of the value of the Kikeout reservoir. But the evidence shows that such reservoir property is a mere site, not useful or used at all in supplying water at present, and possibly never may be. The complaint which the companies make is that only one-half of the value of this reservoir was taken in consideration. Under the circumstances as disclosed by the evidence, the allowance of one-half its value was all the prosecutor is entitled to, and is, we think, unobjectionable from any point of view."

In Chesapeake & Potomac Telephone Company of Virginia v. Commonwealth, 136 S. E. 575, decided January 20, 1927, the Supreme Court of Appeals of Virginia upheld the Corporation Commission in excluding from the

rate base of the telephone company a valuable corner lot purchased for telephone purposes but not yet put in use. President Prentis for the court said (at page 579):

> "Among the items of property which the company claims should be included in the rate base is a valuable lot upon the corner of Seventh and Grace Streets, Richmond, which was purchased three years ago, on December 4, 1923, at a total cost of $286,475.33. This area, excepting a small strip used as an alley, is not now used for any telephone purpose. Part of it is occupied by old residences, and part of it is vacant. The estimate of the present value of this particular lot, exclusive of the use of the alleyway, by a witness for the company, is $319,185.50, and by another expert witness a larger amount. The company contemplates ultimately using this property for telephone purposes. It is adjacent to a valuable building heretofore constructed and now so used. It is said that the company will probably start with that project within the next two years. The forethought which led to the purchase of that property is commendable, but it is no financial burden, for it is shown to be rapidly increasing in value. We think that the Commission did not abuse its discretion in holding that this property is neither used nor useful in the public service, and therefore that its cost should form no part of the present rate base. To hold otherwise would be to charge the public with rates based thereon. It must have some annual value, and the additional profit to the company from its rapidly increasing fee simple value is surely sufficient immediate reward to the company for its foresight. It has no proper place in the rate base valuation upon which the company is presently entitled to receive additional rates from the public for telephone service. The Commission has therefore deducted the price of this property from the estimated rate base."

Re Grangeville Electric Light & Power Company, P. U. R. 1922 D, 513, decided June 24, 1922, was an electric rate case before the Idaho Public Utilities Commission. The proposed rate increases were disapproved. On the subject of excess cost of dam construction, the Commission said (at pages 520-521):

* * * * *

"This Commission cannot presume to take over the management of applicant's property, nor dictate to applicant as to method of construction or amount of expenditures but neither can it permit the applicant to earn a return on an injudicious or unreasonable investment. The applicant may, through a vision of future development of territory, and business to be attached, or for some other reason, have felt fully justified in building for the future, but, if so, it must be satisfied to await such development and additional business for return on investment over that reasonably necessary and required to provide for the demands of the present and immediate near future. In the light of the facts before the Commission, and considering all the circumstances surrounding and conditions relating to the rebuilding of said dam, including the demands of existing service, the Commission believes that there is an excess of cost in said dam over the immediate or near future demand of applicant's service of $115,304.05 which, while a real value, is not now and will not be for a considerable time used and useful in service and therefore must be considered as inoperative property until such time as the demand requires the installation of other generating units and we therefore deduct the sum of $115,304.05 from the value found in establishing the value of the property now used and reasonably necessary and required in the service of the public to be used as a rate base."

In the case of the Columbus Gas & Fuel Company, No. 5635 P. U. R. 1933A, 337, decided in October, 1932, by the Public Utilities Commission of Ohio, the Commission held that only the operated or drilled acreage was "used and useful" and excluded all the undrilled and proven acreage.

The operated or developed acreage which the Commission included consisted of 291,386 acres. The Commission arrived at the number of acres by multiplying the number of wells, which was 3,659 by 79.7 which was the number of acres which the Commission considered one well would develop.

The acreage which was disallowed by the Commission was 2,252,791 acres. This was excluded on the ground that it was undeveloped and therefore not "used and useful."

The Company valued this excluded acreage at $24.752,000.00.

The Ohio Commission valued the operated or developed acreage at $25.00 per acre.

In deciding this case the Ohio Commission held that the present rate payer should not be penalized by a higher rate to take care of a future rate payer.

The expense of rentals on unproducing leases was disallowed, but the Commission held that when this acreage became producing the expense of these leases, including carrying charges should be added and capitalized and go into the valuation.

City of Erie v. Public Service Commission, 278 P. 512, 123 Atl. P. U. R. 1924 D, 89, decided January 1, 1924.

was an appeal from the superior court affirming an order of the Pennsylvania public service commission in a natural gas rate case. The main controversy was over gas holding, which were included in the rate base at a valuation nearly $6,000,000 lower than the lowest estimate of their value shown by the testimony in the case *** On the subject of the property to be included in the rate base, the court said:

> "The Commission correctly summarized the law in these words: 'Gas holding should be included and evaluated only to the extent that they represent *developed, used and useful territory,* including a reasonable reserve for the continued functioning of the company in its public service.'"
>
> * * * * *
>
> "*However, the present value of all the property is not necessarily to be considered in the rate base.* Generally speaking though property may have the value claimed, if a reasonable proportion of its energies or the used and useful property *is not devoted to public service,* it should not ask the consumer to pay a return on the *excess not used in public service,* allowing, of course, for a reasonable *reserve.*
>
> * * * * *
>
> "There can be no graduated values of gas lands fixed as a rate base under any theory presented to us that will consider property presently used and a descending ratio until exhaustion appears that is not the result of the pure guess. Beyond that proportion of the *lands reasonably necessary to the company's life, the rate payer should not be required to assume the remainder as a burden.* Though this may be difficult to determine, the commission, acting as an administrative body in each case, must decide the question, as in all other matters subject to the right of appeal."

* * * * *

"One thing of importance must not be lost sight of. Whether the gas lands be valued or considered on a reservoir or acreage basis, the gas is not paid for as gas until it is brought to the surface and used. In addition to the fair return on the rate base as found there is added payment for the corpus of the estate taken away, or gas that is taken out, used, and cannot be replaced. This is taken care of in an allowance for 'depletion.' The fair return on the rate base is a fair return to the company for the money invested."

* * * * *

"The purchase of additional gas rights, treated as 'operating charges,' places on the present-day consumer an undue burden, particularly when the prices paid are high. It enables the company to recoup immediately its capital outlay. If, in addition, we carry forward the cost as a part of the rate base, or recovery is permitted through depletion, then we allow an additional return on capital already in the pockets of the owners."

* * * * *

"While some rules as to lands for future use must prevail, its determination is primarily for the commission."

(Italics added)

In the case of Logan Gas Company v. Public Utilities Commission of Ohio, 169 N. E. 575, the Supreme Court of that state approved the findings of the Commission, which included the value of leases having producing gas wells drilled thereon, and which rejected and excluded from the rate base all leases under classes 2, 3, and 4, being leases on which there was no development. The court said:

"As to class No. 2, to-wit: Leases or tracts of land proved by actual developments and operations in the immediate vicinity thereof to be good gas-producing lands, *but which do not have any producing wells drilled thereon*, the majority of the court is of the opinion that while these leases upon territory of such character may in the future be 'useful', the same do not come within the purview of the statute which requires the property to be given valuation to be both 'used' and 'useful'.

"The leasehold covering such character of territory not being both 'used' and 'useful', the commission's views upon that point are affirmed."

(Italics added.)

United Fuel Gas Company v. Public Service Commission of West Virginia, 14 Fed. (2d) p. 209:

This was on a bill in equity before a three-judge court to enjoin the Commission from enforcing its order with reference to rates for gas, on the ground that by the orders of the Commission complainants property was being taken from it without due process of law. The court made detailed findings and denied the application for an interlocutory injunction.

The principal issue was the value of the gas leases. The Gas Company controlled the production of natural gas from 814,910 acres of land.

The lower court included in the rate base the assessed value of only 136,384 acres (proven), which were then being used in production, and excluded on the ground that they were not presently used and useful in the public service, 126,208 acres described as probable, and

552,319 acres classed as improbable or unfavorable, valued by the Gas Company at $26,000,000.00.

In the decision by Rose, C. J., it was said:

> "Among the questions raised by the claim of the plaintiff, that the value of the gas under the various classes of acreage shall be *treated as a part of* the value *upon which* it is entitled to a return are:
>
> First, What is the amount of gas under each class?
>
> Second, What is its present value?
>
> Third, How much of that value is presently used in the public service?" (Italics added.)

In discussing these questions the lower court further said:

> "Its right to relief is nevertheless absolutely dependent upon its being able to maintain the position that it is entitled to a fair return upon the present value of such of its property as is *used and useful* in the public service. Whether it showed good judgment in acquiring and holding any other property is irrelevant to any issue upon which it here seeks a decree. No part of the gas which is supposed to be under the acreage classed as either probable or possible is '*used*' in the public service or for that matter in any other, in any ordinary sense of that word."

> "It will be noted that the total of the gas underlying the proven acreage was 249,100,100 M. c. f. As the plaintiff sells annually about 47,000,000 M. c. f. of which 10,500,000 goes to the West Virginia retail purchasers, it has under its proven territory gas enough for everybody for more *than five years*, and an amount sufficient to meet the needs of its public service patrons along for almost a quarter of a century."

"For the reasons already stated, we cannot see how any other portion of its gas can be held to be used in the public service, no matter how elastic a definition be given to the word 'used'. At the risk of tiresome repetition, we can say that we do not criticize the plaintiff for acquiring any or all its gas rights. It was doubtless wise to get them. All that we decide is that, in arriving at the rate base upon which plaintiff is entitled to a fair return, we may not combine two opposing theories. We are not justified in saying that, because plaintiff's investments in gas reserves were prudent, those reserves immediately went into use, and that, therefore, plaintiff is entitled to have them appraised at the many times higher value it says they now have. If, in dealing with its tangible property, and going concern value, we are required to ignore, except for check purposes, plaintiff's investment in them, we must apply the same rule to its gas reserves."

It will thus be seen that the court decided squarely that only the developed acreage should be included in the rate base, and excluded from the rate base 80 per cent of the Company's acreage, valued by it at $26,131,865.00.

The decision of the three-judge court, denying an interlocutory injunction, was affirmed by this court, United Gas & Fuel Company v. Public Service Commission of West Virginia, 278 U. S. p. 322, 73 Law Ed. (U. S.) p. 402.

In United Fuel Gas Case, the reserves of the Company were 249,100,000 M. c. f. and its annual requirements were 47,000,000 M. c. f. In other words, the reserve alloted to the Company was sufficient for only five years. In the instant case the gas reserves in the used

and useful territory was 783,442,000 M. c. f. and the Company's highest requirement per year for produced gas (excluding the purchased gas) is 34,401,978 M. c. f., and this reserve is sufficient for twenty-two years.

We submit that the Commission was justified by the facts in holding that only 71,267 acres of its gas reserves (which are in addition to its purchase contracts, covering 782,421 acres and 1,502 wells, with a potential of 1,532,625 M. c. f.) per day, are used and useful to the Company's rate payers. This allotment includes not only all of the Company's developed acreage and wells, but also 28,970 acres of undeveloped acreage, 27,910 acres of which is in the proven sweet gas area of the Amarillo field. We contend that the fact that the officers of the Company have testified that they consider all of the 1,262, 361 acres held by the company as necessary for its future requirements, is not sufficient to overcome the actual facts, as shown by the undisputed evidence of the Company, that the acreage found as used and useful is sufficient for all of the Company's requirements (on the basis of its greatest demands) for 22 years in the future. We believe that it is not just to require the present consumers to pay for gas reserves which are not now used, and which will not be called for use (if ever) until the distant future.

We respectfully submit that the finding of the Commission that only the value of 71,267 acres designated by it should be included in the rate base and that the value placed on this acreage by the Commission at $2,874,390, should be sustained.

HYPOTHETICAL PIPE LINE.

The Company introduced an exhibit prepared by the chief engineer for Ford, Bacon and Davis, purporting to show the cost of acquiring the reserves, constructing and putting into operation a substitute for the present pipe line system. The testimony pertaining to this exhibit is to be found on pages 533 to 538 of the record.

The witness testified that the hypothetical pipe line system is comparable to the present system only in that it will serve the same markets; that no check of the present system was made to find out whether it had more or less capacity.

He testified further:

> "That no consideration was given to gas supplies in Kansas and Oklahoma; that in designing an actual project any available gas closer than Texas would be taken into consideration. That the witness did not attempt to design a project contemplating any supply of gas from Kansas or Oklahoma and could not estimate the difference in price without refiguring the entire project." (R. 354, 533)

The Commission upon consideration of the evidence pertaining to the hyopthetical line was of the opinion it should be given no weight because in preparing the hypothetical pipe line no consideration was given to the fact that 50 per cent of the pipe line company's supply of gas was obtained in Kansas and Oklahoma, near the market, and because of the failure to give consideration to local gas. The engineer provided for two parallel 24 inch lines from the Amarillo field, while on account of local

gas only one line and that a 20 inch line is now present in the system from the Amarillo field. There was no occasion for construction of two 24 inch lines to the Texas field in view of the fact that the Company had a large amount of local gas available in Kansas and Oklahoma. This hypothetical pipe line covers a different plan and a different system and was more expensive to construct because the engineer in his estimate, went farther than necessary to obtain the gas.

Assigned Error No. 5.

PRESENT VALUES AND PRUDENT INVESTMENT

The Majority Court found that:

> "The present values are on the extensive constructions of the last few years, less than the prudent investment therein." (R. 302)

We do not so understand the evidence.

Exhibit 82 which is set out in the record, throws some light on this comparison.

COMPARISON OF COSTS ON CONSTRUCTION OF WICHITA-OTTAWA 20 INCH LINE.

	As per Company J. O. 12145	As per Black and Veatch	As per F.C. Hamilton Valuation
1. Materials	$2,129,143.27	$.....	$.....
Freight	38,202.17	.....	.....
Warehouse Expense	602.20	.....	.....
	2,167,947.64	2,029,812	.....
2. Labor	806,310.82	.....	.....
Garage, teaming and trucking	9,797.92	.....	.....
	816,108.74	1,008,340	.....
	$2,984,056.38	3,038,152	3,572,723
3. Right of way and damages	58,427.40	54,489	191,775
A	$3,042,483.78	$3,092,591	3,764,498
4. Engineering	302,768.30	154,630	*178,636
B	.....	.....	$3,943,134
5. Legal	2,150.49	**61,852	***19,715
Expense Accounts	11,783.71)		
Incidental Expense	4,378.92)	.....	****39,431
Telephone	744.15)		
B.	$3,364,309.35	$3,309,073	$4,002,280
6. Interest	24,444.01	198,544	320,182
Totals	$3,388,753.36	$3,507,617	$4,320,460
Deduct items not charged to main line construction	$ 13,643.26	.....	.....
	$3,375,110.10	$3,507,617	$4,320,460

* 5 per cent of line B column "Hamilton" x $3,572,723
** Calculated at 2 per cent of A column "Black & Veatch, and includes administration expense x $3,092,591.
*** One-half of 1 per cent of line B column "Hamilton" x $3,943,134.
**** Applies to $3,943,134 at 1 per cent. (R. 425-426)

This comparison covers the construction of one of the Company's major projects before decline in prices and shows the actual cost of the Wichita-Ottawa line was $3,375,110.10 and that Black included the line in his appraisal at $3,507,617, and Hamilton included it in his valuation at $4,320,460.

The exhibit shows the actual cost of materials, freight and warehouse expense was $2,167,947.64, while Black included for the same items of cost, $2,029,812.

The actual cost of labor, garage, teaming and trucking as shown by the books, was $816,187.04, while Black included the same items in his appraisal at $1,008,340.

A comparison of labor, garage, teaming and trucking costs to the Company with Black's value shows that Black valued these (items at $192,232 more than the actual cost to the Company. The contractor who laid this line for the company testified that he lost approximately $128,000 on this contract, (R. 420) and under the contract he furnished the labor, teaming, etc. This substantiates to a large extent Black's value, which is $192,232 more than the actual cost.

Hamilton's valuation did not show a breakdown of the above items; his total value for them is $3,572,723, compared with Black's value of $3,038,125, and the actual

cost of these items, as shown by the books of the Company, of $2,984,056.38.

Right of way and damages on the Wichita-Ottawa line cost $58,427.40, according to the books of the Company. Black included $54,489 for right of way and damages, while Hamilton included $191,777 for the same items.

Engineering expense on this line, including Henry L. Doherty and Company's 5 per cent fee, cost $302,768.30, according to the books. Black allowed for engineering on this line $154,630, while Hamilton included in his percentage allowance for engineering $178,636.

Legal, miscellaneous, incidental expenses and telephone expenses charged to this line on the books of the Company amounted to $19,057.27. Black allowed $61,852 for these items in administration expenses, while Hamilton included $59,146 for comparable items.

The books of the Company show that interest during construction of this line amounted to $24,444.01, which is slightly over 7/10 of 1 per cent of the total cost. Black allowed $198,544 for interest and Hamilton allowed $320,182 for the same item.

We will now leave comparisons of specific construction projects and discuss a comparison of the total present values with the historical values.

A comparison of the values found by the engineers with the book value of the properties is not reliable because there have been writeups on the plant and investment account which were not present in the original investment.

The amount of this writeup could not be ascertained but Exhibit 9 was introduced before the Court showing a writeup of over $9,148,627 in the case of the Kansas Natural Gas Company alone, which was one of the five companies in the consolidation making up the present Cities Service Gas Company.

The exhibit is referred to in the record as follows:

"The annual reports of the Kansas Natural Gas Company filed with the Department of State of the State of Kansas for the years ending December 31, 1921, introduced as Exhibit 8, and December 31, 1922, introduced as Exhibit 9, show the resources, liabilities, capital and reserves of this company at the above stated dates as follows:

	Dec. 31, 1921	Dec. 31, 1922
Total Resources	$12,922,834.61	$23,443,210.00
Liabilities	1,785,551.21	2,572,838.63
Capital Stock	7,700,250.00	6,000,000.00
Surplus	740,522.50	1,568,243.84
Reserves	2,687,510.90	13,302,128.53
Total Liabilities, Capital & Reserves	$12,922,834.61	$23,443,210.00

"'Total Resources' includes the book value of plant investment which was $11,241,229.97, at December 31, 1921, and $20,389,857.72 at December 31, 1922, an increase of $9,148,627.75.

"No new capital was paid in; the combined capital and surplus was less at December 31, 1922 than it was at December 31, 1921." (R. 533)

The total plant investment and other assets including leases of the Cities Service Gas Company is shown to be $96,795,538. This figure includes some leases later sold to the Texoma Company. (R. 375) After deducting the value of the leases sold to the Texoma Company, in the amount of $846,217, (R. 372), the total plant investment and other assets including leases is $95,949,321.

When the writeup of which we have knowledge in the amount of $9,148,627 is deducted we have an historical cost of $86,800,694. Reducing that figure by 10 per cent to arrive at the depreciated value for the purpose of comparing it with the depreciated value found by the Court, we have a depreciated value of $78,120,625.

The Court found a present depreciated value of $82,380,583, which is $4,000,000 more than the historical value or prudent investment value depreciated. Even when an addition is made for Going Value the two figures remain comparable.

Approximately $46,000,000 of this historical value, or actual cost, was added to the plant during the years 1926 to June 30, 1931. (R. 533) This period represented the peak of high prices.

We submit that the present values as found by the engineers are as great or greater than the prudent investment or original cost to the Company when consideration is given to the writeups on the books of the Company. The least that could be said is that the evidence more nearly supports the majority Court's statement in its finding XII that:

"The original cost, or prudent investment, in the pipe line Company's properties is somewhat obscure." (R. 301)

than the positive statement in its finding XIII that:

"The present values are, on the extensive constructions of the last few years, less than the prudent investment therein." (R. 302)

Assigned Error No. 6.

CONCLUSION AS TO VALUATION.

The Commission found a depreciated value of $73,170,510 as of September 1, 1931. (R. 374)

The Commission depreciated overheads. It is stipulated by the parties that overheads should not be depreciated because no annual allowance was provided for overheads.

Accordingly there should be added to this value on account of depreciation of overheads the following:

Engineering and Superintendence during Construction	$ 337,585
Administration and Legal Expense during Construction	36,010
Miscellaneous Construction Expense	72,019
Taxes During Construction	97,127
Interest During Construction	468,652
Total	$1,011,392

When these are added this makes a total depreciated value as of September 1, 1931 of $74,181,902.

We submit that the value of all the Company's properties did not exceed this amount on that date.

Although the valuation was made by the engineers in the summer of 1931, they did not use depressed prices then prevailing.

Black testified:

> "It was not my idea in making this appraisal or fixing these prices to use rock bottom prices of labor or material." (R. 374)

The rate of earned income during the test period in this case was abnormal, the lowest in the experience of the Company, yet the rate base to which it was applied was calculated on normal prices.

In the case of Los Angeles G. & E. Corp. v. Railroad Commission, 289 U. S. 287, the Supreme Court said:

> "It is apparent that the estimates of cost of reproduction new of 1929 or of 1930 upon which the Company relies, afforded no secure foundation for predication of future values, and the rate base as fixed by the Commission is not to be invalidated as involving confiscation by reason of these estimates which the course of events deprived of credit as truthworthy prophecies."

RATE BASE DURING EACH ANNUAL TEST PERIOD.

There should be included in the rate base for any period only the value of the property used and useful in earning the net income during such period.

The test period used in the present investigation covered the years 1930 to June 30, 1932.

Earning statements were submitted for yearly periods as follows:

Year ending Dec. 31, 1930.
Year ending Dec. 31, 1931.
Year ending June 30, 1931.
Year ending June 30, 1932.

The investigation was started in the summer of 1931.

From finding of the Commission it appears that the anticipated test period when the investigation was started was the year ending December 31, 1930, and the year ending June 31, 1931.

The statement of the Commission is as follows:

> "At the suggestion of the Company, the two periods used was the year ending December 31, 1930 and the annual period ending June 30, 1931." (R. 168)

However, before the hearing was completed six months had expired and the Company submitted an earning statement for the last six months of 1931. Before the rehearing was completed another six months had expired and the Company submitted an earning statement for the first six months of 1932.

The Commission then used the full test period agreed upon and also the annual period ending June 30, 1932.

The Court in its findings abandoned the original test period and used the annual periods ending June 30, 1931, and June 30, 1932, although it found that 1932 was an abnormal year and stated:

> "We agree with the Commission that 1932 should not be taken as a test year, for it marks, it is hoped,

the low of the depression through which we are passing." (R. 314)

Since November 30, 1926, the date of the organization of the Company, the plant investment has increased over $46,000,000. During this time its large gas reserves were acquired and a 20-inch pipe line was constructed from Amarillo, Texas to Wichita, Kansas. A trunk line was constructed from Hutchinson to Nebraska, and an additional trunk line was laid from Ottawa, Kansas to Kansas City, Mo., and trunk lines were extended into Missouri.

It is obvious that a comparison of net income during 1930 with the value of property used and useful as of September 1, 1931, would furnish no indication of the net return earned during 1930 on the value of the property used and useful during that year, as large additions were made to the property currently during all of that period as well as during the period from December 31, 1930, to September 1, 1931. It must be presumed that additions to the properties were made for the purpose of securing additional revenues or bringing about economies in expenses.

In determining the return earned on property used and useful during 1930, the value of the property used and useful during that period must be found. The only evidence from which such finding may be made consists of the value at September 1, 1931, as testified to by the engineers, and the cost of the net additions from January 1, 1930, to September 1, 1931, as shown by

the books and records of the Company. In the absence of any very radical change in price levels during the period mentioned, the actual cost of the net additions should compare with the value of such additions at September 1, 1931. Therefore the value of the property used and useful during 1930, which produced the net income earned during 1930, may be fairly ascertained by deducting from the value at September 1, 1931, the net additions from January 1, 1930, to September 1, 1931, and adding to such value of January 1, 1930, the average additions during 1930.

The cost of reproduction new, exclusive of gas leases at September 1, 1931, as found by the Commission is $78,171,761.

The record shows the additions made to the investment in the plant on the books of the Company during the test periods used in the investigation as follows:

Net Additions to Fixed Capital:

July 1, 1931, to Sept. 1, 1931	$ 1,362,506
January 1, 1931, to June 30, 1931	777,591
July 1, 1930, to Dec. 31, 1930	10,471,653
January 1, 1930, to June 30, 1930	592,021

(R. 165)

In the absence of any radical change in price levels during the periods the actual cost of the net additions should compare within reason with the value of such additions as included in the valuations at September 1, 1931. This comparison should be particularly apt in view of the fact that the engineers did not use "rock bottom prices."

In determining the value of the property used and useful in each of the annual periods prior to September 1, 1931, the Commission deducted from the value which is found at September 1, 1931, the additions made during the respective prior periods and then found the average value during such annual prior periods by adding the value at the beginning and end of each year, dividing it by two and applying the percentage condition of 89.94 per cent found by the Commission on the testimony of the engineers to be the per cent condition at September, 1931, and then adding the value of the gas leases which was calculated as the same for all periods.

The following values were found for the respective periods:

Year ending Dec. 31, 1930	$ 66,294,147
Year ending June 30, 1931	66,912,061
Year ending June 30, 1932	73,148,510

(R. 56)

The Commission based its calculations on the rate base as found by it after depreciating overheads and it has been stipulated that overheads should not be depreciated. In addition the Commission made an error in adding to materials and supplies. We have adjusted the figures of the Commission to take care of these ommissions and this adjustment in which we have included the value for the year ending December 31, 1931, is as follows:

Year ending Dec. 31, 1930	$ 67,183,628
Year ending June 30, 1931	67,808,300
Year ending Dec. 31, 1931	73,205,808
Year ending June 30, 1932	74,181,902

The manner in which the Commission arrived at the values for the respective periods has not been challenged.

The Company does however, challenge the figures which the Commission used in making the deductions, which were taken from the Company's books.

The Company contends that all of the property included in the rate base as of September 1, 1931, was constructed and in service during all the test period, but had not been carried to the books and placed in the plant and investment account. According to their theory the new construction was carried on the uncompleted job orders for a considerable length of time after the construction was completed.

The testimony will be found on pages 517 to 528 of the record.

All of the testimony was to the effect that there was a large amount of construction completed in the fall of 1930, which was within one of the test periods.

The Commission was not satisfied with the Company's explanation that the construction was completed long before an entry was made on the plant and investment account. The books show the contrary.

The accountant for the Commission presented an exhibit showing the plant and investment account and the uncompleted job orders during the period covered by the investigation.

The correctness of the audit is admitted by the partie (R. 374)

For the convenience of the Court, the audit of the two

accounts for the year 1930 and the six months period ending June 30, 1931, is here set out:

> "The book value of the plant and property of the Company including completed and uncompleted projects was as follows:

"January 1, 1930.

Plant and Investment Account	$83,223,644.18
Uncompleted Job Orders	3,866,372.39
Total	$87,090,016.57

December 31, 1930.

Plant and Investment Account	$95,828,568.34
Uncompleted Job Orders	2,936,895.73
Total	$98,765,464.07

June 30, 1931.

Plant and Investment Account	$96,795,538.93
Uncompleted Job Orders	2,208,457.57
Total	$99,003,996.50

(R. 527, 528)

The Investment in Plant and Property increased from June 30, 1931, to September 1, 1931, the date of the valuation in the amount of $1,362,506. (R. 526-7)

The majority lower Court, in Finding No. XVI, after having found the annual net operating income of $8,401,680 by averaging the operating income for the two years ending June 30, 1931, and June 30, 1932, stated:

> "The Commission still further increased this by assuming that the income of 1931 was earned upon a lesser investment in the properties; accordingly the Commission deducted from its value as of September 1, 1931, net additions to capital as disclosed by the

Company books from January 1, 1930, to September 1, 1931. But this is shown to be inaccurate because additions were not charged to capital until long after the addition was in service; a lag of from one to three years was customary in order to close up all claims growing out of a particular job. During 1931 there was almost no construction; there was some during 1930, but part of that was to replaace existing facilities. There is evidence that there were not to exceed $2,000,000 additions to plant in the test period; and this would be more than offset in the decline of values between 1930 and the date of the valuations." (R. 315)

We respectfully urge that the majority lower Court misinterpreted the evidence as to the amount of additions to plant in the test period, and was confused by the testimony as to the lag occuring between the time the additions were constructed and the time they were placed in the plant and investment account.

The Company books show the Plant and Investment Account

On June 30, 1931,	$96,795,538,
and at the same date the uncompleted job orders,	2,208,457.
Total of the two accounts, June 30, 1931,	$99,003,995.

The Company contends that there was a lag in the uncompleted job orders and that in truth and in fact the $2,208,457 of uncompleted job orders was in operation at the end of the year 1930, and the Company witness, Eastman gives oral testimony to show such lag by stating that all such uncompleted job orders shown on the book account as such on June 30, 1931, were completed and in

operation in 1930. Eastman stated that there was a lag of from one to three years. (R. 517)

The fallacy of such testimony is shown by the 1930 figures herein before set out.

On January 1, 1930, there was on the books in uncompleted job orders, only $3,866,372. Now if there had been no new construction in 1930, and at the end of the year 1930 there were no uncompleted job orders, then it would show that there was a lag on all of such $3,866,372 cost of uncompleted job orders for a year or a portion thereof, and the plant investment account would have increased in the same amount, to wit, $3,866,372.

Furthermore, if the uncompleted job orders increased during 1930, it would have shown new construction and also a lag, but in fact the uncompleted job orders in the year 1930 decreased $929,477, leaving at the end of the year uncompleted job orders in the amount of $2,936,895.

The record shows also that the plant and investment account at the end of the year 1930 had increased from where it stood January 1, 1930, to wit, $83,223,644
until at the end of the year 1930 it stood $95,828,568
Result—an increase in plant investment of $12,604,924

Thus it follows that the $12,604,924 plant investment account increase less the $924,477 uncompleted job order decrease, or sum of $11,675,447 was new job orders and construction begun, completed and entered in the plant and investment account on the books in the year 1930.

Clearly therefore, the Commission was right when it refused to give weight to the oral testimony in the face of the books records on the plant and investment account.

Comparable figures for September 1, 1931, cannot be given because the amount of uncompleted job orders at that date is not in the record. (R. 527-8)

The books having definitely shown that there was $11,675,447 construction during 1930 which was begun and completed, taken through the job orders and on to the plant and investment account in less than a year's time, the oral testimony pertaining to the lag was destroyed and the facts justified the Commission's finding that all of the property was not constructed and in service during the test period. The Company's challenge of the figures which the Commission used in arriving at a rate base for each of the years, and the Court's conclusion as to their inaccuracy thus failed.

NET INCOME BEFORE DEPRECIATION AND DEPLETION.

There is no dispute as to the net income before depreciation and depletion except as to an item of $50,000 for the year ending June 30, 1932, which the Company adds to expense for the purpose of amortizing rate case expense. At the hearing before the lower Court, there was a controversy as to expense because of payments to Henry L. Doherty & Company. The lower Court found the Doherty payments had not been justified by the evidence. There has been no appeal taken from that part of the Court's findings and decree and the controversy is therefore eliminated.

The agreement of the parties as to net income will be found on pages 515-516 of the record.

The net income before depreciation and depletion for the years covered by the test period is shown by the following table:

Year ending Dec. 31, 1930	$8,904,503.04
Year ending Dec. 31, 1931	8,297,060.35
Year ending June 30, 1931	8,810,691.18
Year ending June 30, 1932	7,963,813.98

To the net earning above set out have been added the payments which were made to Henry L. Doherty & Company and deducted by the Company through expense. (R. 516)

Also to the earnings for the year ending June 30, 1932 has been added the $50,000 deducted by the Company for the purpose of amortizing rate expense.

The only evidence justifying any addition for amortization of rate expense was the fact that the Commission taxed $66,935.08 as costs to the distributing company respondents. (R. 58) There was no evidence in the record of any expense to the pipe line company on account of any rate hearing.

ANNUAL DEPRECIATION AND DEPLETION REQUIREMENTS.

ANNUAL DEPRECIATION.

The agreed statement pertaining to annual depreciation allowance is set out on pages 511 to 513 of the record.

The Company presented evidence and exhibits setting forth the amounts claimed for annual depreciation of each classification of physical property. The Commission accepted the percentages contended for by the Com-

pany and applied them to the present cost of production new as found by it. By applying these percentages to the values, the Commission found that the annual allowance for depreciation of physical properties would be $1,894,022, based on the physical property values at September 1, 1931. The Commission then applied the annual allowance for depreciation set forth above to the physical property values which it found at September 1, 1931 and arrived at a weighted average rate of 2.96 per cent. This is accepted by the parties in the agreed statement as follows:

> "The Commission used an average of 2.96 per cent for annual depreciation on all physical properties, which is accepted by the parties." (R. 512)

ANNUAL DEPRECIATION FOR YEARS COVERED BY EARNING STATEMENT.

The Commission found that because of the recent extensive construction of the Company, all of the physical properties as valued by it on September 1, 1931, were not in service during the years covered by the earning statement as has been discussed heretofore.

As pointed out in the discussion relating to the rate base and the values which should be included in the rate base for comparison with the rate earned during a stated period, the annual allowance for depreciation should be based upon the average value of the physical properties used and useful during each of the earning periods considered.

Applying the agreed rate of 2.96 per cent to the reproduction cost new found for each of the periods under

consideration results in the following allowances for annual depreciation of physical properties:

Year ending Dec. 31, 1930	$1,693,312
Year ending June 30, 1931	1,712,216
Year ending Dec. 31, 1931	1,862,784
Year ending June 30, 1932	1,894,022

It is our contention that the Commission's method of calculating the annual requirements for depreciation during each of the years is logical if the property was not constructed so as to be in service during the years used as a test period, and that no allowance for depreciation should be made in excess of the amounts set forth above for the respective periods.

ASSIGNED ERRORS Nos. 15 and 16.

Annual Depletion Requirements—Gas Leases.

By assigned Error No. 15, appellant complained of the allowance of $329,917.00 as an annual replacement requirement on account of rentals on non-producing leases, (Finding No. 16), and by Assignment No. 16, it complained on account of the findings of the Court and its allowance of $174,747.74 as an annual allowance for dry hole expenses.

The Company claimed an annual allowance for annual reserve requirements pertaining to Gas Leases, as follows:

General development expense capitalized	$532,530.77
A mortization of nonproducing leases	314,981.68
Dry-hole expense	174,747.74
Depletion of producing leases	70,509.88
Total	$1,092,770.07

This large annual depletion requirement which the Company claims for gas leases, is due largely to the fact that the Company carries 998,278 acres of prospective leases which are not even proven to be capable of producing gas and which in most instances are so far removed from the pipe line that they are not available to the present system.

The accounts entering into the depletion requiremnets will be discussed in their order.

ASSIGNED ERROR No. 15.

General Development Expense—Capitalized.

The Company claimed an annual reserve allowance of $532,530.00 for general development expense capitalized.

Eastman testified that this item includes the following character of expenditures: cost of acquiring leases; geological expenses; lease rentals.

The cost of acquiring leases was made up of salaries and expenses of men engaged in acquiring leases and scouting expenses.

The item of $532,530 represents the expenditures for leasehold development charged to capital investment during 1930. These general development expenses are capitalized.

The above amount is estimated as the future annual expenses for leases for those purposes. The Commission in their valuation of leases have included not only the cost of leases but in addition all expenses for geological investigation, scouting and other expenses in pro-

curing said leases and, in addition to this, have included an enhanced value as of September 1, 1931, in the valuation which they have fixed as the fair market value of these leases as of that date. If the Company were allowed this amount as an annual expense and in addition a return is allowed on the value of the leases, which includes these expenditures, there would then be a duplication of charges, that is, the expenditures would be included in the expenses in the first instance and included in the rate base for return in the latter, and we believe that all of this amount should be disallowed.

The Court found with the Commission that no annual allowance should be made for the cost of acquiring leases and geological expenses but allowed $329,917 as an annual replacement requirement on account of rentals on non-producing leases. (Finding No. 16, R. 314)

The Commission allowed only $1,060 for this account. (R. 160)

The difference or increases is $328,857 over the allowance by the Commission. The effect of this increase by the Court is to reduce the net income of the Company in the sum of $328,857.

(The evidence as to this account is found at record page 514.)

Leases such as are owned by the Company require the payment of yearly rental until a producing oil or gas well is drilled, such rental amounts to from fifty cents to one dollar per acre per year, for both the oil and gas rights. The allowance of $329,917 made by the Court includes all of the 1,262,361 acres of Gas Leases, of which

only 42,297 acres are developed and producing gas. In the leases held by the Company on which rentals are required to be paid there are 123,440 acres in the Hugoton field which are more than 90 miles from any pipe line of the Company. They cannot be used until a pipe line is constructed which would be such a major change as to change the entire system of the Company. There are also included nearly a million acres of "prospective" or wild cat leases which are scattered, whose value, if any, is for oil and not for gas.

However, if the contention of the State that but 71,267 acres of these gas leases are devoted to public use and entitled to become a part of the rate base, then this amount should be reduced to cover rentals on only that part of "used and useful" leases for which the Company will be required to pay an annual rental.

Producing leases pay no annual rental. The compensation for such leases is the royalty, which is included in expenses by the Commission and the Company. Inasmuch as in the acreage assigned to the Company as "used and useful" 42,297 acres are developed and producing gas, there will be no annual rental requirement for these leases. This leaves, out of the 71,267 acres of leases assigned as "used and useful" 28,970 acres which are not developed and not producing gas. Of these, 27,910 acres are in the sweet proven area of the Amarillo field. They are part of the blocked acreage in the Burnett lease, and are part of the 50,000 acres in the Burnett lease assigned to the Company in the Amarillo field. As we have seen, the Company is required to pay

$50,000 per year as an annual guaranteed royalty in lieu of an annual rental for the acreage covered by the Burnett lease. (R. 479) This annual guaranteed royalty is charged by the Company as an expense of operation, so that the Company will be required to pay no annual rental on account of this undeveloped acreage in the Amarillo field the annual payment of $50,000 guaranteed royalty for the Burnett being in lieu of such rental.

This leaves the 1,060 acres of probable leases in Kansas, Oklahoma and Missouri; as the only leases on which an annual rental is required to be paid. This rental will not exceed $1.00 per acre per year and if the contention of the State is sustained that only the 71,267 acres of leases assigned by it are entitled to go into the rate base then the full requirement for rentals for non-producing leases will amount to not more than $1,060 per year, and there should be added to the net annual income available for return as found by the Court, $328,857.

We respectfully submit that the allowance by the Court should be reduced to $1,060.

Amortization of Non-Producing Leases.

Under this heading the Company sought to include in its annual reserve allowance $314,981.68 for amortization of non-producing leases, which it claimed was necessary to amortize the cost of leases owned by the Company which were not producing. For example: In the case of a ten year non-producing lease, one-tenth of its purchase price is to be charged to expense each year

until the expiration of the lease or until a well is drilled, which is to amortize its cost over the period of its life of ten years in case of a ten-year lease. This figure of $314,981 is taken from the books and covers the experience of the Company for the year 1930. The Company thus seeks to have included in expenses, as an annual reserve allowance, the cost of these non-producing leases, and it also seeks to have the value of these leases included in the rate base upon which to earn a return.

The present fair value of the used and useful leases is included in the valuation of the Company's property in the rate base on which the Company will be allowed a return. The present fair value of these leases, as found by the Commission, includes not only the cost, the bonus paid, scouting, etc., but also the additional enhancement in value caused by their appreciation as of September 1, 1931. This, in most instances, is many times the actual cost of the lease. There is, in fact, no depreciation or depletion of an undeveloped lease until it has been drilled and commences to produce gas. As soon as a lease becomes productive an annual expense for depletion is then allowed and provided for under amortization of producing leases. In the meantime if an allowance should be made for amortizing nonproducing leases, the Company would be allowed a return not only on the cost but upon the full fair value of these leases, and it is seen, therefore, that by this contention the Company is seeking to have returned both the cost of the leases through an annual reserve charge and at the same time a return on the fair market value of the leases.

We believe that no reserve allowance should be made so long as the leases are nonproductive. If the Company were allowed for amortization purposes one-tenth of the value of these nondeveloped leases annually, then after five years, it would have had returned to it one half of the fair value of the lease and thus the present consumers would be required to pay for the amortization of these leases and also a return on their full value, although they would have received no gas and no benefit from them. We believe that if the consumers are required to pay a rate for gas based upon fair value of its property, including the fair value of these leases, they should not at the same time be required to pay for the amortization of non-producing leases which are not in fact being depleted by use. If the lease through development becomes productive, annual depletion is then allowed in an item of depletion of producing leases.

The Court agreed with the contention of the Commission and disallowed this item. (Finding 16, R. 317)

ASSIGNED ERROR No. 16.

Dry Hole Expense.

This account is intended to cover the future annual expense of the Company in drilling dry holes upon its leases.

The Commission, for this requirement, allowed $12,000.00.

The Court allowed $174,747.74. (Finding 16, R. 317)

The difference is $162,747.74. The allowance by the

Court is the amount claimed by the Company and is based upon the experience of the Company for the year, 1930.

During the years, 1929 and 1930, the Company was engaged in acquiring its leases and in so doing was required to scout, to drill wells, to determine and locate the gas producing areas and to test those leases procured, by development. During this time many new gas fields were discovered, many of which were considerable distance from the Company's pipe line.

In 1930, the Company drilled ten dry holes on scattered acreage in Oklahoma and Kansas, and one well in Texas, none of which was drilled upon the territory classified herein as "proven".

The Company now has ample proven gas reserve sufficient to last it for many years in the future and its period of scouting and its period of pioneering is past.

The testimony of all of the witnesses, both for the Company and the State, is to the effect that in the area classified as proven, there is little or no likelihood of encountering a dry hole in the development of this proven territory. The evidence discloses that in the proven Sweet gas area of the Amarillo field that no dry hole has yet been encountered.

Because of the above testimony the Commission valued the leases as proven gas leases on which no dry holes would probably be drilled; if the probability of dry holes existed the Commission would have found a lower value because of this contingency.

We contend that it would be unsound to make a material allowance for the future for annual expense for dry holes, when the testimony shows that the used and useful leases are proven. The Commission allowed $12,000.00 for this account which is the average cost of drilling a dry hole. The evidence showed that a dry hole cost from $3,000.00 to $21,000.00, depending upon the area.

If the contention of the state is sustained that there should go into the rate base only the 71,267 acres which the Commission has assigned to the Company as its leases which are devoted to the public use, then a *fortiori* the allowance claimed by the Company and allowed by the Court is excessive, for in this "used and useful" acreage there are only 28,970 acres which are undeveloped, and of this amount 27,910 acres are in the Sweet proven gas area of the Amarillo field, and only 1,060 acres are probable.

We therefore, submit that in any event the annual allowance for dry holes should not exceed the sum of $12,000.00 allowed by the Commission, and that there should be deducted from the amount allowed by the Court the sum of $162,747.74.

Annual Requirement for Depletion of Producing Leases.

The Company claims an annual allowance of $70,509.58 for depletion of its producing leases. The testimony of Eastman, for the Company, was that this figure was arrived at by the operating department, based upon geological information and operating records, but

that he was unable to tell how this amount was arrived at or give a breakdown of this amount, and no information as to how this amount was calculated or arrived at has been given to the Commission.

This amount was accepted by the Commission as correct.

We therefore respectfully submit that the reasonable allowance for annual reserve requirements pertaining to gas leases is as follows:

General Development Expenses Capitalized	$ 1,060
Dry Hole Expense	12,000
Depletion of Producing Leases	70,509
Total	$83,569

which figure should be added to the annual depreciation pertaining to physical equipment for the purpose of obtaining the total allowance for annual depreciation and reserve requirements.

ASSIGNED ERROR No. 18.

FAIR RATE OF RATE RETURN.

The Court erred in its finding and conclusion that approximately 8 per cent return upon the present valuation is necessary for The Cities Service Gas Company at the present time, and that a return substantially lower than that would be confiscatory; (R. 317) and erred in its finding that if abnormality is considered the return must be increased and not decreased. (R. 318)

The evidence pertaining to a proper rate of return will be found on pages 528 to 533 of the record.

For the convenience of the court we are setting out in the brief herein some of the evidence as to the rate of return:

"Testimony in regard to a proper rate of return was given by the witnesses F. C. Hamilton, P. McDonald Biddison and Charles F. Clark for respondents and by C. H. Montgomery for the Commission."

The witnesses for the Company testified that under present conditions a fair rate of return should be in excess of 8 per cent. Montgomery for the Commission testified that a fair rate of return for the Cities Service Gas Company would be from 6 to 8 per cent, and that 8 per cent would be the maximum in normal times.

Through a witness for the Company, "testimony was introduced to the effect that because of the assistance of the holding company, the Cities Service Company, the Cities Service Gas Company has been able to sell its securities at an 'interest rate that was from a half to three-fourths per cent less than anything else that was put out at about that time on a similar project', and in addition to that it gets better terms on its mortgages. It does not have to pay them off in ten years as many of the pipe line companies have had to do with issues that have been put out in the last two years. Because of this, the Cities Service Gas Company was able to sell its 5½ per cent bonds for 96¼.

> 'The company, having ample financial resources, does not necessarily have to issue securities now or six months from now or two years from now. They pick and choose their time when the markets are right.'" (R. 530)

We admit that excessive past profits cannot be used as a gauge for future rates. For the purpose only of throwing some light on what return may be expected for the Company in the future, we submit a resume of the Company's financial history.

"Montgomery's Exhibit 49 shows the financial history of the pipeline system under consideration beginning with the organization of the Cities Service Gas Company to date. The Cities Service Gas Company was organized in the latter part of 1926, acquiring the assets and assuming the liabilities of the following companies:

Empire Natural Gas Company
Kansas Natural Gas Company
Empire Gas and Pipe Line Company
Kansas-Oklahoma Gas Company
Empire Gas & Fuel Company (Delaware)
(Gas properties only.)

"The stock control of these companies had been theretofore acquired by Cities Service Company and their assets were acquired and liabilities assumed by the Cities Service Gas Company as of November 30, 1926. Balance sheets of the companies at the time of consolidation are shown on pages twenty-four and twenty-five of Montgomery's Exhibit 49.

"These balance sheets show that at the date indicated the book value of the plant investment of the companies, including uncompleted job orders, was $52,182,525.98, and that reserves for depreciation and depletion had been accumulated out of earnings in the amount of $22,423,936.95. These reserves which had been accumulated out

of earnings amounted to 42.97 per cent of the plant investment.

"These balance sheets show that the companies had accumulated a surplus amounting to $14,903,660.21, which sum is equal to 87.26 per cent of the total capital stock of the companies taken over.

"The combined reserves for depreciation and depletion and surplus amounted to $37,327,597.16, which is equal to 218.55 per cent of all outstanding capital stock of the companies and 71.53 per cent of the plant investment.

"In the case of the Empire Natural Gas Company, it had a capital stock of $10,574,000 and compared to such capital stock it had surplus of $6,066,436 and reserves for depreciation and depletion of $10,192,715, a total of surplus and reserves of $16,259,151, which is equal to 153.77 per cent of its capital stock.

"The plant investment of the Empire Natural Gas Company, including uncompleted job orders, as reflected in the books of the company as of November 30, 1926, was $26,577,355; its reserves for depreciation and depletion amounted to $10,192,715, which is equal to 38.35 per cent of the plant investment.

"In the case of the Kansas Natural Gas Company it had a capital stock of $6,000,000 and surplus of $7,784,067 and had accumulated reserves for depreciation and depletion amounting to $11,905,381. Its surplus amounted to 129.73 per cent of its capital stock and the combined surplus and reserves amounted to 198.42 per cent of its capital stock. The book value of its plant

investment was $18,861,223, including uncompleted job orders, and its reserves for depreciation and depletion of $11,905,381 was 63.12 per cent of such plant investment.

"The Empire Gas and Pipe Line Company had a capital stock of $5,000 and surplus of $907,323, which was 18,146.46 per cent of its capital stock. Its reserves for depreciation and depletion was $325,840, making the combined reserves and surplus $1,233,163, all of which was accumulated on a capital stock of $5,000.

"The plant investment of the Empire Gas and Pipe Line Company, including uncompleted job orders, was $1,625,569, compared with combined surplus and reserves of $1,233,163.

"The financial history of the company since the consolidation in November, 1926, may be found on pages 1 to 8, inclusive, in Exhibit 49, which reflects the combined operations of the Cities Service Gas Company, the Cities Service Gas Pipe Line Company and the American Pipe Line Company.

"It is shown that surplus has been accumulated, in excess of all interest and dividends paid, of $9,044,629 to June 30, 1931; its depreciation and depletion reserves have increased to $10,818,020. Its total assets have increased from $60,595,001 as of December 31, 1926, to $109,431,039 as of June 30, 1931. [During this time its outstanding stock and bonds increased only $28,365,700 and its loans only $9,000,000.]

"The Cities Service Gas Company has during all this time paid interest on its bonds and dividends on its

capital stock; in 1928 it paid $1,000,000 dividends, and in 1929 and 1930 it paid $2,000,000 each on dividends, which is at the rate of 8 per cent per annum. Its earnings before interest (and depreciation) were as follows:

1927	$5,335,739
1928	6,053,621
1929	8,660,793
1930	8,829,480
Twelve months ending June 30, 1931	8,741,809

"The net profit of the companies, after paying all interest charges available for reserves and common stock during each of the years 1927 to 1930, was:

1927	14.99%
1928	13.12%
1929	21.25%
1930	19.97%

"Its net return after paying all interest and other charges and providing substantial allowances for depreciation and depletion amounted to the following percentages of its outstanding capital stock during each of the years 1927 to 1930, inclusive:

1927	9.96%
1928	6.75%
1929	14.53%
1930	10.82%

"Page 1 of Exhibit 49 shows that the book value of plant investment, including uncompleted job orders, increased from $53,243,126 as of December 31, 1926, to $99,003,996 as of June 30, 1931, an increase of $45,760,868." (R. 530-2)

The First paragraph of Finding No. 18 of the Lower Court is as follows:

> "A return of approximately 8 per cent upon present values is necessary, under present conditions, to assure confidence in the financial soundness of the Cities Service Gas Company, to maintain its credit, and to enable it to raise money necessary for the discharge of its public duties. Any return substantially lower than that would be confiscatory. (United Railways v. West, 280 U. S. 234, 252.) (R. 317)"

Since the majority of the lower court based this finding upon the West Case, supra, a comparison of the facts in that case with the case at bar is appropriate.

In the West case, page 281, appears the following:

> "There is much evidence in the record to the effect that in order to induce the investment of capital in the enterprise or enable the company to compete successfully in the market for money to finance its operations, a net return upon the valuation fixed by the Commission should not be far from 8 per cent. Since 1920 the company has borrowed from time to time some $18,000,000.00 upon which it has been obliged to pay an average rate of interest ranging well over 7% and this has been the experience of street railway lines quite generally."

In the case at bar it is apparent that the affiliation and mutual assistance rendered by the great and efficient Doherty organization that this particular plaintiff is and has been able to sell its securities at an "interest rate that was from a half to three-fourths per cent less than anything else that was put out at about that time on a similar project, and that it gets better terms on its mortgages. Because of this situation it was able

to sell its 5½ per cent bonds for 96¼. This plaintiff having ample resources does not necessarily have to issue securities now or six months from now or two years from now. It picks and chooses its time when the markets are right." (R. 530).

The record shows this plaintiff sold twelve million dollars of first mortgages, pipe-line 6 per cent gold bonds at par. It is apparent, therefore, that it is able to obtain funds at a very low rate and is assured of financial stability and a supported credit which enables it to raise all necessary money for the proper discharge of its duties at a low rate of interest. It is apparent also that there is little risk or hazard in its business. The pipe line system which it has established is a permanent fixture for an indefinite period. It has a gas reserve which insures it of a supply of gas lasting well into the future. The territory which it serves is well protected; it has almost a monopoly on the territory which it serves due to the fact that the distributing units are affiliated companies and it would be economically unsound for another pipe-line company to invade its territory.

It appears from the evidence that the Company is fully financed and its system construction completed.

In the West case, page 251, we find the following:

> "Upon the valuation fixed, with an allowance for depreciation calculated with reference to that valuation, and upon the then prescribed rates, the company for the years 1920 to 1925, both inclusive, obtained a return of little more than 5 per cent per annum."

In the case at bar the net profit after paying all interest and other charges providing for substantial allowances for depreciation and depletion amounted to the following percentages of its outstanding capital stock during each of the years 1927 to 1930 inclusive.

1927	9.96%
1928	6.75%
1929	14.53%
1930	10.82%

In the case at bar, furthermore, in the year 1928 the company paid interest on its bonds and dividends on its capital stock, the dividend amounting to $1,000,000.00 and in the year 1929 paid interest on its bonds and dividends on its capital stock amounting to $2,000,000, and in the year 1930 paid interest on its bonds and dividends on its capital stock of $2,000,000, the dividends amounting to 8% per annum, and during the period the plant investment, including uncompleted job orders, increased from $54,243,128 on December 31st, 1926, to $99,003,996 on June 30th, 1931, an increase of $45,760,872.

In the case at bar in the majority opinion of the lower Court in its finding No. 12 appeared the following:

> "The Cities Service Gas Company was organized in 1926. It took over the physical properties of five pipe line companies having a plant investment account, at the time, of $52,182,325.98." (R. 301)

The record discloses that at that time in those companies reserve for depreciation and depletion had been accumulated out of earnings in the amount of $22,423,936.95 or 42.97% of the plant investment and at that time

these companies had accumulated a surplus amounting to $14,903,660.21, equal to 87.26% of the total capital stock of all the companies taken over.

When this company was thus organized and its books opened $17,080,000 of the capital stock and $2,000,000. of bonds became immediately $25,000,000 worth of common stock and $25,000,000 of 5½% bonds. The reserve for depreciation and depletion above set out in the amount of $22,423,936.95 became only $7,760,706 and none of the surplus of $14,903,660.21 above set out was carried over into the new corporation. (R. 173)

On June 30th, 1931, they had built up a surplus of $9,044,629, after having paid all of the dividends hereinabove referred to and the interest on the bonds. (R. 531)

In addition to paying the bond interest and the dividends above referred to the company loaned other affiliated companies $7,559,571. (R. 173)

The net earnings before interest and depreciation in

1927	5,335,739
1928	6,053,621
1929	8,660,973
1930	8,829,480
12 months ending June 30th, 1931	8,741,809

(R. 532)

In the case at bar it will thus be seen that the Cities Service Gas Company is one of the large system, and organized among other purposes for the purpose of maintaining the credit of subsidiary companies and it has been able to do that and conducted its business so as to meet its demands, to pay its operating expenses in-

cluding interest on bonds, to pay a dividend of 8% on its capital stock and in addition thereto to accumulate a surplus of $9,044,629 and its depreciation and depletion reserves have increased $10,818,020 since 1926. (R. 173)

In the West Case in the opinion on page 249 appears the following:

> "What is a fair return within this principle cannot be settled by invoking decisions of this court made years ago based upon conditions radically different from those which prevail today. The problem is one to be treated primarily by present day conditions. Annual returns upon capital and enterprise, like wages of employees, cost of maintenance and repleted expenses, have materially increased the country over. This is common knowledge. A rate of return upon capital invested in street railway lines and other public utilities which might have been proper a few years ago no longer furnishes a safe criterion either from the present or the future."

In the case at bar the very opposite exists. Annual returns upon capital and enterprise, like wages of employees, cost of maintenance and related expenses, have materially decreased the country over. This is common knowledge.

In Finding No. 18 in the majority opinion of the lower court appears the following:

> "There is evidence that in years past, the profits of the company exceeded 10 per cent."
>
> "We do not analyze those figures. *** " (R. 318)

We believe that consideration should be given to the experience of the recent past for the purpose of determining requirements for the future.

In the case at bar, furthermore, Judge Hopkins in his dissenting opinion cites the case of Wabash Valley Electric Company, vs. Young, 77 L. Ed. 348, 287 U. S. 488, and quotes from the opinion by Mr. Justice Southerland as follows:

> "It is true, as appellant points out, that in United Railways v. West, 280 U. S. 234, 251-252, this court held that a rate of return for a street railway of less than 7.44 per cent was confiscatory, saying that sound business management required that after paying all expenses of operation, etc., 'there should still remain something to be passed to the surplus account,' and that a rate of return which did not admit of that being done was 'not sufficient to enable a utility to maintain its credit and raise money for the proper discharge of its public duties. Many cases were cited tending to show that a return of 7½ per cent, or even 8 per cent, might be necessary, but it was said (pp. 249-250) that no rule could be laid down which would apply uniformly to all sorts of utilities. 'What may be a fair return for one may be inadequate for another, depending upon circumstances, locally and risk.' A street railway company compelled to meet the growing competition of private automobiles, public omnibuses, and other motor carriers, well might sustain such losses of revenue because of the decreased number of passengers carried, as to require a larger rate of return than would be required by an electric company like appellant, which not only enjoys a practical monopoly in the field where its services are rendered, but whose financial structure, it fairly may be assumed, is greatly strengthened by its affiliations and by the interested support of the parent company to which it belongs. On the whole we are unable to conclude that a 7 per cent rate of return, under the facts here disclosed, is so law as to be confiscatory. See Smith v. Illinois Bell Telephone Co. Supra, at pp. 160-161."

Furthermore in the case of Wabash Valley Electric Company vs. Young, Supra the following appears in the opinion, on 77 L. Ed. page 354; 287 U. S. 448, 501:

> "The testimony for appellant was to the effect that to take care of bonds, debt discounts, borrowed money and stock dividends a return of 7 per cent was sufficient; but that in order to accumulate a surplus and make it easier to finance the company, the rate of return should be not less than 8 per cent. Appellant's balance sheets show that on January 1, 1929, it had an accumulated surplus of $1,074,739.71, and, at the end of that year a surplus of $1,257,884.64, as compared with a total stock and funded debt liability of about $4,500,000. The record, as already stated, also shows that appellant is a subsidiary of the Central Indiana Power Company by which it is owned and financed, its securities having been taken directly by that company without any intervening agency. The power company also own and finances the other affiliated corporations in the same way. It is reasonable to conclude that appellant is in a more favorable financial condition than if it were a disconnected enterprise."

The Supreme Court in the recent case of Los Angeles G. & E. Corp. v. Railroad Commission, 289 U. S. 287, in its opinion said:

> "The Commission calculated that the Company would have a return of 7 per cent on this rate base.
>
> * * * * *
>
> "And we recognize that a rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market and business conditions generally. See Smith v. Illinois Bell Teleph. Co., 282

U. S. 133, 160, 161, 75 L. ed. 255, 269, 270, 51 S. Ct. 65. Applying these principles, and considering the financial history of the Company, its relations and opportunities, and the general situation as to investments, we find it impossible to hold that a return of 7 per cent is so low as to be confiscatory."

In Finding No. 18, the majority Court states as follows:

"The witness for the Commission testified that 8 per cent would not be an unreasonable return in normal times, but testified that these times are abnormal, as they are. But if abnormality is considered, the return must be increased, not decreased. In these times when stock of the best utilities can be purchased on a 9 per cent basis or better, certainly an 8 per cent return on this hazardous enterprise is not unreasonable." (R. 318)

We cannot fathom the reasoning of the Court underlying this finding.

It is a very general principle of law that a public utility is entitled to earn such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties. The country has entered upon a changed economic level. We submit that it is common knowledge that under the present depressed and abnormal conditions, the earnings of the best organized and best financed concerns of the country are decreased and many of them are not even earning operating expenses. Rates

of interest on borrowed money are the lowest in the history of the country.

The Court designates this Company as being engaged in a hazardous enterprise, but its history is one of successful and profitable business with no real competition to meet in its field of service. The Company's pipe line system is entirely completed. It is fully financed, its market is assured and has existed for many years; it has practically a monopoly upon the territory which it serves for the reason that no other like company can afford to expend the enormous amounts of money necessary to invade its territory. It has an almost unlimited supply of gas; it deals in a commodity which is a household necessity. We submit that it is not now a hazardous enterprise.

In finding No. 12, the majority Court found:

> "Electricity supplanted gas for lighting and is making serious inroads on cooking, while fuel oil is proving a formidable competitor for heating." (R. 301)

Yet the record in this case shows that in the year of organization it produced and purchased 45,550,572 M.c.f. of gas, and in the test year 1930 it produced and purchased 74,163,945 M.c.f. In the first six months of 1931 it produced and purchased 34,547,379 M.c.f. (R. 491) In the year of 1930 the amount of gas it sold for other purposes was twice that sold for domestic use. There is no evidence in the record to support the Court's finding.

In abnormal times such as these we are now experiencing, a concern that is able to show any profit is the exception and even the strongest concerns in any business are contented and indeed fortunate if they can show a return of 6 per cent.

We believe that the fact that depressed conditions caused the decrease in earnings in 1931 and 1932 should be given consideration in determining a rate for the future.

The net income of the Company under investigation, before depreciation for the year ending December 31, 1931, shows a decrease of $707,434, as compared with the previous year. The net income for the year ending June 30, 1932, shows a decrease of $896,878 as compared with the previous year. (R. 515) This decrease is due almost entirely to the loss in sales of industrial gas during the present industrial depression. (R. 178) Unless it is to be assumed that the present economic conditions are to continue indefinitely, this decrease is abnormal and must be given consideration in using present earnings as the test for the future rate.

It is also true that the rate in controversy pertains only to domestic sales. The loss in income during the test period is due almost entirely to industrial sales. During the year 1931 as compared with 1930 domestic sales increased 686,310 M.c.f., while industrial sales showed a decrease during 1931 as compared with 1930 of 3,375,194 M.c.f. (R. 179) We believe that the Company should be required to carry part of the burden

due to loss in industrial sales pending the adjustment of the economic conditions and not place it all on the domestic consumer.

Considering the favorable position which the Company has financially, the support which it receives from affiliated companies, the assured market which it has for its gas, its gas reserves which insure its supply, its financial experience in the past, and the present economic conditions, we believe that a 6 per cent return is adequate.

EFFECT OF COMMISSION'S ORDER ON INCOME.

The order of the Commission was to the effect that the contract under which the Cities Service Gas Company sells gas to the distributing companies at the city gate at an average price of 39.5 cents per M.c.f. was unreasonable and that any payments made by the distributing companies in excess of 30 cents per M.c.f. should not be allowed as an operating expense. (R. 61)

The order in no way affected the price at which industrial gas was being sold. It pertained only to town border sales for distribution to domestic consumers.

In order to have some test by which to estimate the effect of the Commission's order it was agreed that,

> "The rate established by the Commission in its order Exhibits L — H if applied to the business of the Cities Service Gas Company for the year ending June 30, 1932, would result in a reduction of earnings of $1,926,145.07." (R. 372)

We have accepted the figure for the purpose of estimating the rate of return which the Company would earn under the Commission's order.

We do not concede however that the loss in income would have been $1,926,145.07 during the year ending June 30, 1932, if the Company had been operating under a 30 cent rate. If the Company's rate is reduced to 30 cents we believe that the amount of gas sold for domestic purposes will increase, and the increased consumption will increase the income of the Company.

Gas in the territory sold by the Company has become a household necessity. Wood and coal cannot compete with gas if the cost to the consumer is placed on a comparative basis. A reduction of the gas rate to 30 cents would no doubt greatly increase the consumption of domestic gas and the net return to the company might be sufficiently increased to make up the reduction in the gate rate.

ASSIGNED ERRORS 14, 17, 19.

RATE OF RETURN UNDER COMMISSION'S 30 CENT ORDER.

The anticipated test periods, when the investigation was started in the summer of 1931, covered the two annual periods ending December 31, 1930, and June 30, 1931. Before the hearing was completed six months had expired and the Company submitted an earning statement for the last six months of 1931. A rehearing was had and before it was completed another six months had

expired, and the Company submitted an earning for the annual period ending June 30, 1932.

The Commission then used the full test period agreed upon and also the annual period ending June 30, 1932, although it found:

> "That it would be inequitable to accept this figure of reduction in earnings without taking into consideration that reproduction costs new at this time would also cut valuations fixed by the Commission in its original opinion substantially." (R. 60)

The majority Court in its findings abandoned the original test period and used the annual periods ending June 30, 1931, and June 30, 1932, although it found that 1932 was an abnormal year. In using the earning statement from the annual period reflecting this decrease in earnings, the lower Court gave no consideration to the fact that prices for labor and material had also dropped which would have materially affected the rate base.

We have discussed under separate headings, the valuation of the properties entering into the rate base and the net additions made to plant and equipment during the annual periods covered by the test.

We have also discussed under separate headings, the Company's annual income, and depreciation and depletion requirements for each annual test period.

The reduction resulting from the Commission's order when tested by the sales in the past is agreed to be $1,926,145.07.

For the purpose of showing the effect of the Commission's order on the rate of retun, we have compiled a

table showing the rate base, net income before depreciation and depletion, the annual depreciation and depletion requirements, reduction in revenue under Commission's order, net income under Commission's order and the rate of return for each annual period covered by the investigation.

The table follows:

CITIES SERVICE GAS COMPANY.

NET INCOME, RATE BASE AND RATE OF RETURN FOR EACH ANNUAL TEST PERIOD.

	Dec. 31, 1930	June 30, 1931	Dec. 31, 1931	June 30, 1932
Net Income before depreciation	$8,829,480.71	$8,741,809.14	$8,228,178.30	$7,861,516.85
Add: 1%	75,022.33	68,882.05	68,882.05	52,297.13
Add: Rate case expenses				50,000.00
Total	8,904,503.04	8,810,691.19	8,297,060.35	7,963,813.98
Less: Depreciation	1,693,312.00	1,712,216.00	1,862,784.00	1,894,022.00
Annual Lease Rentals	1,060.00	1,060.00	1,060.00	1,060.00
Dry Hole Expense	12,000.00	12,000.00	12,000.00	12,000.00
Depletion of Producing Leases	70,509.88	70,509.88	70,509.88	70,509.88
Total	1,776,881.88	1,795,785.88	1,946,353.88	1,977,591.88
	$7,127,621.16	$7,014,905.31	$6,350,706.47	$5,986,222.10
Agreed reduction in revenue under Commission's order	1,926,145.00	1,926,145.00	1,926,145.00	1,926,145.00
Net Income under Commission's order	$5,201,476.16	$5,088,760.31	$4,424,561.47	$4,060,077.10
Average Value	$67,183,628.00	$67,808,300.00	$73,205,808.00	$74,181,902.00
Rate of Return	7.74%	7.50%	6.04%	5.47%

As shown by the above table under the Commission's order the Company would have been making approximately 8 per cent return during the year 1930 without giving any consideration to increase in sales which would result from the reduction in the rate.

The return for the year ended June 30, 1931, is 7.5 per cent. A slight decrease is shown. Loss of income from industrial sales is just starting to show its effect.

The return for the year ended June 30, 1932, is 5.47 per cent. The loss in industrial sales due to the present industrial depression had reached the maximum during the test period.

The lower Court found that 1932 was an abnormal year, stating:

> "We agree with the Commission that 1932 should not be taken as a test year, for it marks it is hoped, the low of the depression through which we are passing." (R. 314)

The lower Court however, disregarded its finding, abandoned the original test period, and based its findings on the annual periods ending June 30, 1931, and June 30, 1932.

We contend that the test period used by the majority Court was unfair. We have however prepared a table for the purpose of showing what the results would have been had the Court not erroneously increased the rate base and made depletion allowances for gas leases not used and useful. This calculation covers the same annual periods as used by the Court. The rate base and deprecia-

tion requirements as of September 1, 1931, have been used.

CITIES SERVICE GAS COMPANY.

NET INCOME, GIVING EFFECT TO DEPRECIATION ALLOWANCE ON VALUE AS OF SEPT. 1, 1931, AND RATE BASE OF SEPT. 1, 1931.

	—Year ended—		
	June 30, 1931	June 30, 1932	Average
Net Income Before Depreciation	$8,741,809.14	$7,861,516.85	$8,301,662.99
Add: 1¾%	68,882.05	52,297.13	60,589.59
Add: Rate case expenses		50,000.00	25,000.00
Total	$8,810,691.19	$7,963,813.98	$8,387,252.58
Less:			
Depreciation on 9-1-31 values	1,894,022.00	1,894,022.00	1,894,022.00
Annual Lease Rentals	1,060.00	1,060.00	1,060.00
Dry Hole Expense	12,000.00	12,000.00	12,000.00
Depletion of Producing Leases	70,509.88	70,509.88	70,509.88
Total	$1,977,591.88	$1,977,591.88	$1,977,591.88
Net Income Available for Return	6,833,099.31	5,986,222.10	6,409,660.70
Agreed Reduction in revenue under Commission's order	1,926,145.00	1,926,145.00	1,926,145.00
Net Income under Commission's Order	$4,906,954.31	$4,060,077.10	$4,483,515.70
Value, 9-1-31	$74,181,902.00	$74,181,902.00	$74,181,902.00
Rate of Return	6.61%	5.47%	6.04%

Had the majority Court given effect to its finding that 1932 was abnormal and should not be used as a test period and used the years ending December 31, 1930, and December 31, 1931, a more accurate test would have been obtained. We have made a calculation showing the results as to these periods using the rate base as of Sep-

tember 1, 1931, to make it comparable with the lower Court's findings, although over $11,000,000 of construction was done in 1930 and not in operation during that entire year to produce an income.

The table showing the rate of return for these two annual periods follows:

CITIES SERVICE GAS COMPANY.

NET INCOME GIVING EFFECT TO DEPRECIATION ALLOWANCE ON VALUES AS OF SEPT. 1, 1931, AND RATE BASE AS OF SEPT. 1, 1931, AVERAGE OF YEARS ENDED DECEMBER 31, 1930, and DECEMBER 31, 1931.

	—Year ended—		
	Dec. 31, 1930	Dec. 31, 1931	Average
Net Income before Depreciation.	$8,829,480.71	$8,828,178.30	$8,528,829.50
Add: 1¼%	75,022.33	68,882.05	71,952.19
Total	$8,904,503.04	$8,297,060.35	$8,600,781.69
Less: Depreciation on 9-1-31 values	1,894,022.00	1,894,022.00	1,894,022.00
Annual Lease Rentals	1,060.00	1,060.00	1,060.00
Dry Hole Expense	12,000.00	12,000.00	12,000.00
Lease Depreciation of Producing Leases	70,509.88	70,509.88	70,509.88
Total	$1,977,591.88	$1,977,591.88	$1,977,591.88
	6,926,911.16	6,319,468.47	6,623,189.81
Agreed Reduction in Revenue Under Commission's Order	1,926,145.00	1,926,145.00	1,926,145.00
Net Income under Commission's Order	$5,000,766.16	$4,393,323.47	$4,697,044.81
Value, 9-1-31	$74,181,902.00	$74,181,902.00	$74,181,902.00
Rate of Return	6.74%	5.92%	6.33%

As we have previously stated, the Company was completing pipe line extensions during the year 1930, some of it extending into the year 1931. As this property was not in operation and producing an income during all of the year 1930, we do not believe it proper to include it in the rate base when considering the return during that period.

The following table shows the return earned after making such adjustment:

CITIES SERVICE GAS COMPANY.

NET INCOME, AVERAGE VALUE AND RATE OF RETURN AVERAGE FOR YEARS ENDED DECEMBER 31, 1930, AND DECEMBER 31, 1931.

	Year ended Dec. 31, 1930	Year ended Dec. 31, 1931	Total	Average
Net Income before depreciation	$8,829,480.71	$8,228,178.30	$17,057,659.01	$8,528,829.50
Add: 1¾%	75,022.33	68,882.05	143,904.38	71,952.19
Total	8,904,503.04	8,297,060.35	17,201,563.39	8,600,781.69
Less: Depreciation	1,693,312.00	1,862,784.00	3,556,096.00	1,778,048.00
Annual Lease Rentals	1,060.00	1,060.00	2,120.00	1,060.00
Dry Hole Expense	12,000.00	12,000.00	24,000.00	12,000.00
Depreciation of producing leases	70,509.88	70,509.88	141,019.76	70,509.88
Total	1,776,881.88	1,946,353.88	3,723,235.76	1,861,617.88
	$7,127,621.16	$6,350,706.47	$13,478,327.63	$6,739,163.82
Agreed reduction in revenue under Commission's order	1,926,145.00	1,926,145.00	3,852,290.00	1,926,145.00
Net Income under Commission's order	$5,201,476.16	$4,424,561.47	$9,626,035.63	$4,813,018.82
Average Value	$67,183,628.00	$73,205,808.00		$70,194,718.00
Rate of Return	7.74%	6.04%		6.86%

This shows a return of approximately 7 per cent, and includes the loss in income from industrial gas for the year 1931. If we can anticipate a recovery of industry in the future, the return of industrial sales would bring this return over 8 per cent.

The Commission used the test period which was suggested when the investigation started and included also the year ending June 30, 1932, and found a rate of return slightly below 7 per cent upon its valuation. The Commission however took cognizance of the fact that labor and material prices had declined since the valuation was made by the engineers, and stated that this must be given consideration if the abnormal year 1932 was used in the test period.

The calculation of the Commission adjusted according to the stipulation as to overhead values is as follows:

CITIES SERVICE GAS COMPANY.

NET INCOME, AVERAGE VALUE AND RATE OF RETURN AVERAGE FOR YEARS ENDED DECEMBER 31, 1930, JUNE 30, 1931, AND JUNE 30, 1932

	Dec. 31, 1930	June 30, 1931	June 30, 1932	Average
Net Income before Depreciation	$8,829,480.71	$8,741,809.14	$7,861,516.85	$8,477,602.23
Add:				
1¾%	75,022.33	68,882.05	52,297.13	65,400.50
Rate case Expenses			50,000.00	16,666.67
Total	$8,904,503.04	$8,810,691.19	$7,963,813.98	$8,559,669.40
Less:				
Depreciation	$1,693,312.00	$1,712,216.00	$1,894,022.00	$1,766,516.66
Annual Lease Rentals	1,060.00	1,060.00	1,060.00	1,060.00
Dry Hole Expense	12,000.00	12,000.00	12,000.00	12,000.00
Depletion of Producing Leases	70,509.88	70,509.88	70,509.88	70,509.88
Total	$1,776,881.88	$1,795,785.88	$1,977,591.88	$1,850,086.54
	7,127,621.16	7,014,905.31	5,986,222.10	6,709,582.86
Agreed Reduction in Revenue under Commission's order	1,926,145.00	1,926,145.00	1,926,145.00	1,926,145.00
Net Income under Commission's order	$5,201,476.16	$5,088,760.31	$4,060,077.10	$4,783,437.86
Average Value	$67,183,628.00	$67,808,300.00	$74,181,902.00	$69,724,610.00
Rate of Return	7.74%	7.50%	5.47%	6.86%

At the risk of being tiresome, we have set out these various tables showing the results from the use of the various test periods.

We believe that an accurate picture is presented by them.

Under any of the test periods used, the Company will be making a return of over 6 per cent and if the abnormal year 1932 is eliminated the return materially increases.

DECREASED INCOME DUE TO LOSS OF INDUSTRIAL SALES—VALUE OF DOMESTIC SERVICE.

The Company's loss in income during the period covered by the investigation was due almost entirely to loss in industrial sales. During the same period gas sold for domestic use showed an increase.

During the year 1931 as compared with 1930, domestic sales increased 686,310 M. c.f., while industrial sales showed a decrease during the year 1931 as compared with 1930 of 3,375,194 M. c.f. Domestic sales increased $347,415.85, during the 1931 period compared with 1930 and other sales decreased $957,385.57. (R. 179)

The net income before deducting annual depreciation and depletion requirements, for the first and last annual period covered by the investigation, is as follows:

Year ending:	
Dec. 31, 1930	$8,904,503.00
June 30, 1932	7,963,813.00
Decrease	$ 940,690.00

This shows a loss in income of approximately a million dollars due almost entirely to loss of industrial sales caused by the present financial depression. There was some loss in domestic sales the first six months of 1932 which was largely offset by gains in domestic sales in 1931. Had it not been for this temporary loss in income from loss of industrial sales the Company would be making an unreasonable return under the Commission's order.

The net profits to the Company after paying all interest charges, which were available for reserves and common stocks during each of the years 1927 to 1930 was:

1927	14.99%	1929	21.25%
1928	13.12%	1930	19.97% (R. 532)

If the Company's income is temporarily reduced because of loss of industrial sales, we do not believe the burden of maintaining it should be carried by the domestic patrons.

The evidence showed that in past years the net return after depreciation and depletion requirements of the Company had exceeded ten per cent. As to this evidence the lower Court stated:

> "There is evidence that in years past, the profits of the Company exceeded 10 per cent. We do not analyze those figures; in rate making the past must bury its dead; a confiscatory rate cannot be ordered for the future because an exorbitant profit was made in the past." (R. 318)

With the Court's statement as a general proposition of law we agree, but the Court in applying the law, overlooked the material proposition.

In determining the return which the Company will make in the future it is proper to consider its experience in the past. The past earnings were excessive. The Company's earnings have decreased because of loss of industrial sales. That loss was caused by an abnormal condition. If abnormal, it will improve in the future. If the decrease in earnings due to depressed industrial

conditions is not given consideration the future rate will be unreasonable.

The Commission's order affects only the rate for gas sold for domestic consumption where the rate is in excess of 30 cents per M. c.f.

The temporary decrease in industrial sales has not increased the value of the service to the domestic consumer.

The rights of a particular class of patrons cannot be ignored. A utility should not be allowed to maintain rates that are unjust to one class of its patrons because there has been a temporary loss of income from another. The constitution does not require that temporary loss in income be remedied by imposing an unreasonable burden upon only one class of patrons.

In Covington & L. Turnpike Road Co. v. Sanford, 164 U. S. 578, 41 L. ed. 560, it was held:

> "The interests of the public as well as of the owner of the property must be considered, with all the circumstances, in determining what is a just rate to be charged by a turnpike company."
>
> "The right of a corporation to realize a given per cent upon its capital stock cannot be claimed without reference to the interests of the public. *** " (Syl. 9 & 10)

The test as to the value of the service was stated in Cotting v. Godard, 183 U. S. 79, 46 L. ed. 92, as follows:

> "The question is always, not what does he make as the aggregate of his profits, but what is the value of the services which he renders to the one seeking and receiving such services." (p. 97)

We submit that when consideration is given to the tem-temporary decrease in income due to loss of industrial sales the return to be earned under the Commission's order is ample.

If the rate of return is affected by a temporary decrease in industrial sales the Company should carry part of the burden and not place it all on the domestic consumer because the value of the service to him has not increased.

In Smyth v. Ames, 169 U. S. 466, 42 L. ed. 819, it was held:

> "The public have a right to be exempt from unreasonable exactions; and the interest of the corporation is not the sole test of suitable rates." (Syl. par. 12)

In the opinion, the Court said:

> "What the Company is entitled to ask is a fair return upon the value of that which is employed for the public convenience. On the other hand, what the public is entitled to demand is that no more be exacted from it for the use of a public highway than the services rendered by it are reasonably worth." (p. 547)

ASSIGNED ERROR No. 20.

The Court, in its finding No. 20, found as follows:

> "If the distributing companies are compelled to pay 40 cents per thousand cubic feet for gas at the city gates and to base their rates to the consumers upon the price fixed as reasonable by the Commission, no one of them will have earnings in excess of operating expenses applicable to depreciation and return." (R. 319)

We believe that the finding is outside of the issue herein, and that there is no competent evidence in the record to support it.

The Commission appreciates the fact that before anything can be done in the way of determining the reasonableness of the distributing companies' gas rates to the domestic consumer, a determination must first be made of the reasonableness of the price which they pay to their affiliated pipe line company for gas which they distribute.

There being over one hundred of these separate distributing plants it was not practicable to try the reasonableness of the pipe line company's gate rate separately with each distributing plant. All of the distributing companies being similarly affected, the Commission had a joint hearing of all of the companies for the purpose of determining only the reasonableness of the contracts with the affiliated companies.

At the start of the investigation, the distributing companies raised no objection to the jurisdiction of the Commission to determine the reasonableness of the gate rate charged them by their affiliated pipe line company.

The distributing companies, however, objected to the Commission making any finding as to their several earnings or the several valuations of their property in this joint hearing.

They objected to any evidence being submitted upon these questions, contending that the reasonableness of the gate rate must first be established and that each distributing plant would then have the right to a separate and independent hearing as to the reasonableness of its rate giving effect to the Commission's order as to a reasonable amount which should be paid for gas to its affiliated pipe line company.

Mr. Stone, appearing for the distributing companies, stated as follows:

> "Mr. Stone: Now, if the Commission please, the last paragraph of the citation issued by the Commission contains this statement: 'It is further by the Commission ordered: That each of the above-named respondents appear on the above mentioned date to give to the Commission such information as they may desire on their own behalf, and as may be required by the Commission, in behalf of said investigation, and to show cause why such holding company contracts, or service or commodity charges, should they be (fol 266) found to be unreasonable should not be disallowed as operating expense of the distributing companies, and adjustment made in this respect as to charges made to the consumers.' Now that paragraph, your honors, seems to contemplate that should you find forty cents to be too high at the city gate it should be reduced say to thirty-five cents, or thirty cents, that that reduction of five or ten cents should be immediately adjusted as to each distributing company without any separate hearing as to the needs and requirements of that particular company.

* * * * *

Mr. Stone: Our understanding was that the Commission contemplated proceeding then to make such adjustment without any hearing, and that is why we have filed these appearances as to each company, and I will read it so you may understand our position. Maybe there is no difference.

* * * * *

Mr. Stone: After stating the appearance, we say: 'Said respondent hereby expressly limits its appearance and appears specially for said purposes and said purposes only hereby expressly objecting to any consideration by this Commission in this proceeding of the reasonableness or unreasonableness of its existing rates or any attempt to change the same by reason of any findings which this Commission may make in respect to said contracts from the evidence introduced herein and expressly denying the jurisdiction of the Commission to consider in this proceeding any issue as to the value of respondent's property, the adequacy or inadequacy of its earnings or the reasonableness or unreasonableness of its rates for the following reasons:" (R. 236-7)

It therefore clearly appears that the distributing companies challenged the jurisdiction of the Commission to investigate anything in the joint hearing except the reasonableness of the contracts between the affiliated companies.

Before the hearing closed, the distributing companies attempted to introduce general testimony pertaining to the value of their distributing plants and their income. The Commission sustained the objection to this testimony. The action of the Commission was in conformity with the original position of the companies.

In their bills of complaint before the District Court, the companies complained of the Commission's refusal to allow them to introduce such general testimony and the question went before the District Court in the following manner:

> "It is further stipulated that the witness F. C. Hamilton will testify that if the several distributing companies complainants herein are compelled to pay the price they are now paying the Cities Service Gas Company for gas at their respective city gates and are compelled to base their rates to consumers upon the price fixed by order, Exhibit M, they will not be able to make operating expenses, with nothing for return and depreciation on the value of their property, to which testimony the Commission objects on the ground of incompetency, the subject matter not coming in issue until the Commission has made an investigation for the purpose of determining the fair value of the properties owned by the distributing companies and their rate of return." (R. 371)

Upon this statement alone the Court made its finding 20.

It was conceded by counsel for the Commission before the District Court and is now conceded that the Commission had no authority to order a reduction in the rates of the distributing companies until they were given a separate hearing on the reasonableness of their rates regardless of the reduction in the pipe line rate.

We respectfully submit that the record does not justify such finding by the Court and that the distributing companies' position in requesting it is inconsistent with their position before the Commission.

The only question presented by this controversy is the

reasonableness of the contract between the pipe line company and the affiliated distributing companies. Until the reasonableness of the pipe line company's charge is determined, a finding as to the reasonableness of the distributing companies' expense cannot be made for the purpose of determining a proper rate for them to charge to the ultimate consumer.

ASSIGNED ERROR No. 4.

"The court erred in not accepting the findings of fact, declarations of law, and dissenting opinion of Honorable Richard J. Hopkins declaratory of the law and facts controlled in this action."

Hopkins, D. J., filed a dissenting opinion and findings of fact and conclusions of law. The opinion shows that it is the result of painstaking study and a thorough understanding of the evidence as shown by the record. This opinion adopts the findings of the Commission as to the valuation of the property and the return earned thereon, except two items that did not materially affect the rate base, and concluded that after an investigation of the facts and the law that plaintiffs had failed to show that the order in controversy made by the Public Service Commission of Kansas was unlawful or confiscatory.

We agree with Judge Hopkins that the effect of the reduction of the gate rates would be to increase the amount of gas sold for domestic purposes and to increase the return of the Company. Gas in the territory

served by the Company has come to be a household necessity. No one in its territory would burn wood or coal if he could obtain gas at somewhere near the same cost. A reduction of the gate rate from 40¢ to 30¢ would no doubt greatly increase the consumption of the domestic gas and the net return of the Company and might even increase the return to the Company sufficient to make up the reduction in the gate rate.

Judge Hopkins in his opinion shows careful consideration of the evidence pertaining to the gas leases and going value. The two accounts make up the chief difference between the value found by the Court and that found by the Commission.

After considering all of the evidence on gas leases, he concludes as follows:

> "In my opinion the Commission was well within its powers in finding that 71,267 acres of plaintiffs' gas reserves, which are in addition to its purchase contracts, covering 782,421 acres and 1,502 wells, with a potential of 1,532,625 M. C. F. per day, are used and useful to the company's developed acreage 27,910 acres of which is in the sweet proven gas area of the Amarillo field. The testimony of the officers of the company that they considered all of the 1,262,361 acres held by it as necessary for its future requirements, is not sufficient to overcome the actual facts, that it has an adequate supply for twenty-two years in the future. It would be contrary to common sense and justice to require the present consumers to pay for gas reserves which are not now used and which might never be used for their needs." (R. 331)

His conclusion as to Going Value is also to the point:

> "It is perfectly apparent that both witnesses arrived at their calculations for idle plant upon a hypothetical basis without considering the actual facts and experiences of the company. It appears that the Commission applied the tests which both engineers laid down as a proper measure of determining going-concern value and found that $2,000,000 was sufficient and proper allowance.
>
> The record shows clearly that on the major part of the pipe-line system there was very little idle plant following the construction period." (R. 333)

We also wish to call the Court's attention to Judge Hopkins' conclusion as to the evidence pertaining to the valuation as a whole:

> "The Commission saw and heard the witnesses, painstakingly examined their testimony and with the discretion allowed it under the law, arrived at what it determined the fair and reasonable value of plaintiff's property. And while it is the duty of this court to make an independent investigation of the facts which it has done, this court should be careful not to substitute its judgment for that of the Commission, unless it is clear that the Commission erred. ***
>
> The evidence in my opinion fails to disclose on such items sufficient reasons for setting aside the findings of the commission and substituting those of this court, nor does the evidence justify a finding of this court that a gate rate of 40 cents to the distributing companies is fair and reasonable." (R. 328)

We have, in our brief, called the Court's attention to the failure of the majority lower court to give consid-

eration to loss of industrial sales during the present financial depression.

This was recognized by Judge Hopkins in the following language:

> "In 1930 the effect of the depression began to affect sales and earnings of the company largely through loss of industrial business, a business bound to be regained as industrial business improves; and it goes without saying that the carrying the investment and expense of industrial business should not be placed on the domestic consumer." (R. 326)

With reference to the rate of return and what is fair rate as applied to this company under the circumstances shown in the evidence and as they exist throughout the world at the present time, Judge Hopkins says:

> "We are also confronted with changed conditions affecting opportunity for investment which tends to limit the amount of the return. Annual returns upon the capital have materially decreased in the past two or three years. Business is generally satisfied with a very low rate of return. All businesses, including that of public utilities, are satisfied with a much less rate of return than they were three or four years ago when annual returns upon the capital were unreasonably high."

> "The Cities Service Gas Company is not an ordinary public utility. It is one of a large system organized for the purpose of maintaining the credit of subsidiary companies and assisting them in their finances. It has been able to expand its business so as to meet increased demands, to pay its operating expenses, including interest on money borrowed, to pay dividends of 8 per cent upon its capital stock and accumulate a large surplus. (See Smith v. Illinois Bell Telephone Co., 282 U. S. 159, 161.)" ***

"A return of six per cent is not unreasonable at this time. In fact, the great majority of concerns now doing business are glad to earn as much as five per cent and are fortunate to do so. Even a five per cent return at this time would not be confiscatory."

(R. 335)

This Court will take judicial knowledge that the facts are correctly stated and we submit that the conclusion that Judge Hopkins drew from these facts that

"Even a five per cent return at the time would not be confiscatory."

logically follows.

ASSIGNED ERRORS Nos. 1, 2, 3, 21 AND 22.

We contend in view of what we have said heretofore, that the lower Court was in error; in permanently enjoining and restraining the enforcement of the Commission's order providing that the distributing companies should cease to set up on their books as an expense item any payments made to the Cities Service Gas Company for main line town border gas in excess of 30 cents per M. c. f., and should give no consideration to any such payments in fixing a rate for the domestic consumers; in finding and declaring the order of the Commission was unreasonable and would, if not enjoined, confiscate the property of plaintiffs; in holding that 40 cents per thousand cubic feet for gas at the city gates is a reasonable charge; in its conclusion that the portion of the first order of the Commission made August

31, 1932, providing that the distributing companies should give no consideration to the payment for gas at the city gates in excess of 30 cents per thousand cubic feet in fixing the rate for domestic consumers, should be permanently enjoined; and in refusing to dismiss plaintiffs' bills.

CONCLUSION.

We respectfully submit that the Court was in error in its findings of fact and conclusions of law, and in its failure to dismiss the plaintiffs' bills of complaint.

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LOUIS R. GATES,
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The Supreme Court of the United States

OCTOBER TERM, 1933.

No. 114.

THE STATE CORPORATION COMMISSION FOR THE STATE OF KANSAS, HOMER HOCH, JESSE W. GREENLEAF, ET AL.,
APPELLANTS,

vs.

THE WICHITA GAS COMPANY, HUTCHINSON GAS COMPANY, NEWTON GAS COMPANY, ET AL.,
APPELLEES.

SUPPLEMENTAL BRIEF OF APPELLANTS ON QUESTIONS ARISING ON ORAL ARGUMENT.

STATEMENT.

In our opinion the supplemental brief filed by appellees on the question of jurisdiction tends to confuse the issues and create uncertainty as to the manner in which the investigation was handled by the Commission. We have therefore requested the court for permission to discuss briefly the facts pertaining to these matters, all of which are disclosed by the record.

Appellees express surprise and confusion because of alleged inconsistencies on the part of the Commission

and on the part of the Commission's attorneys. We do not believe it necessary to enter into a controversy as to these expressions. The facts as disclosed by the record show a consistent and orderly procedure on the part of the Commission.

We find it impossible in our reply to follow the order of argument in appellees' supplemental brief because of the manner in which the various theories are comingled. We will therefore discuss in order, the jurisdiction of the Commission, what was done by the Commission and the purpose of the investigation, the jurisdiction of the Federal Court, and what appears to us to be the contentions set forth in appellees' supplemental brief.

JURISDICTION OF THE COMMISSION.

We admit that the Commission is a creature of statute. We do not believe it necessary to go into a lengthy discussion to establish its broad general powers which are common to all such regulatory bodies.

The Revised Statutes of Kansas, R. S. 66-101 conveys general powers as follows:

> "The public utilities commission is given full power, authority and jurisdiction to supervise and control the public utilities and all common carriers, as hereinafter defined, doing business in the State of Kansas, and is empowered to do all things necessary and convenient for the exercise of such power, authority and jurisdiction."

The statute makes it the duty of all public utilities to charge none but just and reasonable rates. (R. S. 66-107.)

In addition to its power to investigate and regulate rates on its own motion, the act specifically gives the Commission authority to investigate on complaint or on its own motion "any regulation, practice or act whatsoever affecting or relating to any service performed by such public utility or common carrier for the public." (R. S. 66-110, 66-111.)

The power of the Commission to correct such regulation, practice or act if found to be improper is provided for as follows:

> "And if it shall be found that any regulation practice or act whatsoever, relating to any service so performed or to be performed by such public utility or common carrier for the public in any respect is unreasonable, inefficient, insufficient, unjustly discriminatory or unduly preferential or otherwise in violation of any of the provisions of this act, or of any of the laws of the State of Kansas, the public utilities commission shall have full power, authority and jurisdiction to substitute therefor such other regulations, classifications, schedules practice service or act as they find and determine to be just, reasonable and necessary." (R. S. 66-113)

This is all in addition to the power given to the Commission to investigate and order substitutions for "rates, joint rates, fares, tolls, charges, rules, regulations, classifications or schedules."

These statutes are set out in full in an appendix attached to this brief.

The broad powers to the Commission were stated by the Kansas Supreme Court in State, ex rel. v. Postal Telegraph Co., 96 Kan. 298, 304 as follows:

"Continuing this examination of later enactments, we find the Commission vested with full power, authority and jurisdiction to supervise and control the public utilities and common carriers, and empowered to do all things necessary and convenient for the exercise of the power, authority and jurisdiction. That is to say whatever power is necessary to the effectual exercise of the specific powers conferred is likewise conferred."

It necessarily results that under the broad supervisory power granted the Commission it was clearly within its jurisdictional authority when it proceeded to investigate the practice of the distributing companies of paying 40 cents to its affiliated company for gas, as a preliminary step in determining the reasonableness of the distributing companies rates to the consumer. This payment for gas made up the material part of the expense of the distributing companies.

There was no other method by which to determine the reasonableness of the contract but a lengthy investigation.

As stated by the Court in its opinion:

"We are of the opinion that the facts here justify the conclusion that the Cities Service Company, together with the Gas Service Company, the distributing companies, the Empire Gas & Fuel Company and the Cities Service Gas Company are engaged in a common enterprise, namely, the transporting and furnishing of gas to local consumers; that the Cities Service Company exercises such complete dominion and control over the Cities Service Gas Company and the distributing companies that, under the general rules of agency, the Cities Service Gas Company and the distributing companies are mere agen-

cies or instrumentalities of the Cities Service Company; and that, in substance and effect, the Cities Service Company is, through such agencies, supplying gas to local consumers on demand and is engaged in a local business." (R. 286.)

The Commission adopted the only practicable procedure. The distributing companies consisted of 135 separate operating units, operating in as many separate cities. They were all similarly affected by the contracts. Only by a joint hearing could all their rights be protected. The companies recognized this before the Commission and agreed to proceed jointly in the investigation of the contracts. (R. 236-7.)

It necessarily results that the first step in the investigation of the reasonableness of the distributing companies' rates had to be a determination of the reasonableness of the affiliated company contracts where they could all appear jointly. This would be followed by a separate hearing as to the reasonableness of the rates of each separate distributing plant which covered matters in which there was no joint interest.

The Commission in its proceedings acted under the authority of the statutes above referred to and the decisions of Smith v. Illinois Bell Telephone Company, 282 U. S. 133, and Western Distributing Company v. Public Service Commission of Kansas, 285 U. S. 119.

PURPOSE OF INVESTIGATION.

It is the contention of the Commission and, we submit the record plainly shows, that the proceeding taken by it was for the purpose of fixing the rates charged by the various distributing companies to their local consumers, in each city in Kansas served by them. That the first step in this investigation required a determination by the Commission of whether certain contracts which were common to all of the distributing companies, to wit the Doherty $1\frac{3}{4}$¢ charge, the Gas Service Company charge, and the gate rate, were reasonable. That the order expressed the Commission's intention, if the investigation showed that any such charge was unreasonable, then as a second step to investigate the rates which each of the distributing companies charged to its consumers, and that the commission proposed after giving effect to the reasonable cost of gas as found and such other reductions as such investigation should disclose were proper, to fix a local rate, for each of said cities.

We think the original order of July 2, 1931, (R. 26) plainly shows this.

After advising that the reasonableness of certain contracts by the distributing companies would be investigated, this order recited that the respondent distributing companies would be required,

> "to show cause why such holding company contracts, or service or commodity charges, should they be found to be unreasonable, should not be disallowed as operating expense of the distributing companies, and adjustment made in this respect as to charges made to the consumers."

On the completion of the first step of this proceeding wherein the reasonableness of the contracts mentioned were investigated, and determined, the Commission made its order of August 31, 1932, Exhibit L, (R. 59,) finding that the Doherty contract and the gate rate of 40 cents were unreasonable, and that a gate rate of 30 cents, was reasonable, and requiring that after September 1, 1932, the respondent distributing companies should cease to set up *on their books* as an operating expense, such payments, and give no consideration to such payments in fixing a rate for the domestic consumer. This order notified the respondent distributing companies

> "That on the 17th day of October, 1932, the distributing companies, respondents above named, appear before the Public Service Commission at 10:00 o'clock A. M., and show cause to the Commission why the reduction in expenses as above set forth should not be passed on to the consumers with such other reductions as may be found reasonable."

We think these two orders plainly show that the purpose of the commission was, if the investigation disclosed the unreasonableness of the contracts under consideration, then as the next step and as a part of the proceeding, that a hearing be had as to each city, to determine from such hearing what the local rate should be for such city after giving effect to its findings and determination as to their said contracts, and that by the order Exhibit L. (R. 62) the respondents were given due notice of such purpose of the Commission, and a full and complete opportunity to be heard on the question as to a proper local rate. And we submit that the permanent injunc-

tion by the District Court prevented the Commission from concluding its investigation.

It is true that on August 31, 1932, the Commission made a second order, Exhibit M, (R. 63,). But this was a mere interim order to remain in force pending the hearing ordered from October 17, 1932, requiring the respondent distributing companies to readjust their local rates at once so as to reflect the elimination of the Doherty charge and the 30 cent gate rate. In making this interim order the Commission assumed, without giving the distributing companies an opportunity to be heard, that the local rates then being charged, would be unreasonable to the extent of the reduction in their operating expenses, caused by the eliminating of the Doherty 13¼% charge and by the reduction of 10 cents in the price for gas.

If this assumption had been determined to be true then we think the Commission would have been justified in making this second order Exhibit M.

The Commission realized however, when this second order was called in question that the respondent distributing companies, had a right to be heard on that question before the order could be made, and that a hearing might disclose in some cases, after giving effect to this reduction in operating expenses, that the local rate, still might not be unreasonable and subject to reduction, and in other cases the hearing might disclose that a reduction of even more than the saving caused by these reduced expenses, would be proper.

For this reason the commission promptly on the application for temporary injunction confessed the illegality of the second order Exhibit M.

It made the same confession in its answer. The Commission does not now complain of the injunction as to the second order.

JURISDICTION OF THE COURT BELOW.

As was stated by counsel for the Commission in oral argument before this Court the Commission has no desire to avoid an early judicial determination of the propriety of its finding as to the reasonableness of the contract for gas at the city gates.

It has however always been the position of the Commission that the Federal Court had no jurisdiction over the controversy because of the absence of a federal question.

The appellees devote much space in their brief as to the inconsistent position of the appellants on this question. The position taken by the appellants before the lower court is a matter of record and does not depend upon conclusions or argument.

In addition to its motion to dismiss because of the absence of a federal question presented and overruled before answer the appellants again presented the question in its answer as follows:

> "These defendants answering further allege that the order issued by the Commission on August 31, 1932, was the reasonable exercise of the jurisdiction conferred upon them by the laws of the State of Kansas, and that the plaintiff has not thereby been denied any of the rights which they may have under the constitution of the State of Kansas or the constitution of the United States.

Defendants admit that that part of its order, Exhibit "M" to plaintiff's bill of complaint, dated August 31, 1932, wherein the defendant commission ordered the distributing companies from and after September 1, 1932, to deduct the excess between what the distributing companies were then paying for gas at the city gate and thirty cents per M. c. f. of gas and pass the difference to the consumer, is null and void, and further allege that these defendants have abandoned said order and allege that said Commission now has no intention of enforcing or attempting to enforce said order; that the defendant Commission relies upon and alleges it has the right to enforce its order made on August 31, 1932, Exhibit "L" attached to plaintiff's bill of complaint, whereby it ordered said distributing companies to show cause why they and each of them should not pass said reduction in price to be paid for gas at the city gate on to the consumers and in this connection these defendants allege that such proceedings contemplate that an investigation be made as required by law as to each of said distributing companies to determine whether the earnings of said distributing company, based upon the fair value of their property are excessive and unreasonable, after giving effect to the said thirty cent gate rate and all other facts bearing upon the question.

Defendants allege that unless and until said hearing is had and these defendants make an order determining that said rate to the consumers be reduced, that its said order, Exhibit "L," will not and may not affect the plaintiff, and that until an order is made reducing said rate to said distributing companies by the consideration of said reduced gate rate this court has not and will not have jurisdiction of the subject matter of this action.

Wherefore Defendants, having answered all and singular those parts of the bill of complaint material and necessary to answer, pray that notwithstanding

they have answered all the allegations of the bill of complaint that the court dismiss the bill of complaint for the reason and on the ground that it plainly appears from the averments therein contained that no federal question is raised by the bill of complaint and this court is without jurisdiction to try the cause." (R. 264, 265.)

The position of counsel in presenting this question to the District Court is also in writing and speaks for itself. In the brief before the District Court it was said:

"The plaintiffs raise three constitutional objections, as follows:

1. Confiscation of property.

2. Interference with the right to contract.

3. Interference with interstate commerce.

An examination of the order clearly discloses that none of these constitutional prohibitions are affected.

All the order does is to find that the contracts are unreasonable, and finds the extent of the unreasonableness.

It does not take any property from the pipe-line company. It continues to collect the same amount. It does not take any property from the distributing companies. They will continue to earn the same amount until a valid order is made requiring them to make an adjustment to the consumer.

The order interferes with no contracts or rights. The distributing companies are not ordered to discontinue the contract nor to discontinue any payments made thereunder. The contract remains in full force and effect. The only thing which the order does is to find that the payments made under the contract are unreasonable. Because of the affiliated relationship, and the fact that all of the net earnings over

and above the interest requirements of both companies pass into the hands of the Cities Service Company, the holding company, there can be no interference with any constitutional right nor privilege until some order is made which in some way affects the companies financially or otherwise. We therefore submit that any order or finding which this court makes in the premises must be a moot issue and upon a matter which does not present an actual controversy."

Without adding to or taking from this statement, we again submit it on the question of federal jurisdiction.

It has never been the thought of the Commission that the companies could not have a judicial review of its preliminary findings and order as soon as made. This remedy was in the state courts, however, and not in the federal, because of the absence of a federal question.

The Revised Statutes of Kansas, R. S. 66-118, provides in part:

"Any common carrier or public utility governed by the provisions of this act, or other party in interest, being dissatisfied with any order of the commission fixing any valuation, toll, rate, joint rate, fare, charge, or findings, rules or regulations, classifications, schedules, or any order or ruling fixing any regulations, practices or service, or order or ruling relating to the issuance of stocks, bonds or other securities hereinafter provided may, within thirty days from the making of such order, commence an action in a court of competent jurisdiction, against the public utilities commission as defendant, to vacate and set aside any such order, finding or decision of the public utilities commission on the ground that the valuation, toll, rate, joint rate, fare, charges, orders, rules, regulations, findings, classifications or schedules in such decisions are unlawful or unreas-

> onable, or that any such regulation, valuation, practice or service fixed in such order or decision is unreasonable."

The statute is set out in full in the appendix.

It therefore clearly appears that had the companies sought a judicial review in the state courts, they had a complete statutory remedy, but instead they sought the jurisdiction of the Federal Court and the absence of federal jurisdiction was disclosed by their own pleadings.

The appellees raised the question in their own briefs as to the moot issue. We do not attempt to master the ingenious argument by which the appellees would give the lower court jurisdiction of the case on its merits and then have the issue become moot so as to prevent a review on appeal. We believe that their rambling argument ends when met with the proposition that under Section 266 of the judicial code the Commission has a right to have reviewed any decree of a District Court enjoining the enforcement or execution of an order issued by it.

The Commission was proceeding on an orderly investigation in accordance with the jurisdiction conferred upon it by the statutes heretofore set out.

It necessarily follows that either the District Court had no jurisdiction to hear the case on its merits, or if it did the appellants have a right to a review on the merits.

If the District Court had no jurisdiction to enjoin the Commission's order, Exhibit L, its decree must of course

be reversed and the Commission permitted to proceed under its valid order.

The Federal Court will not interfere with the legislative process of the Commission except to enforce constitutional rights.

The function of the Federal Court was expressed by Chief Justice Hughes in the recent case of Los Angeles G. & E. Corp. v. Railroad Com., 289 U. S. 287, 304, as follows:

> "We approach the decision of the particular questions thus presented in the light of the general principles this Court has frequently declared. We have emphasized the distinctive function of the Court. We do not sit as a board of revision, but to enforce constitutional rights. San Diego Land & Town Co. v. Jasper, 189 U. S. 439, 446, 47 L. Ed. 892, 896, 23 S. Ct. 571. The legislative discretion implied in the rate making power necessarily extends to the entire legislative process, embracing the method used in reaching the legislative determination as well as that determination itself. We are not concerned with either, so long as constitutional limitations are not transgressed. When the legislative method is disclosed, it may have a definite bearing upon the validity of the result reached, but the judicial function does not go beyond the decision of the constitutional question. That question is whether the rates as fixed are confiscatory. And upon that question the complainant has the burden of proof and the Court may not interfere with the exercise of the State's authority unless confiscation is clearly established."

The right of the company to object only to confiscation regardless of the Commission's procedure was stated by

Justice Butler in the case of United Fuel Gas Co. v. Railroad Comm., 278 U. S. 300, 309, as follows:

> "The contentions also that the commission was not lawfully created under provisions of the state Constitution, and that its order was void because not supported by findings, have the same and no greater force than the objection that the rate is confiscatory. Suitors may not resort to a court of equity to restrain a threatened act merely because it is illegal or transcends constitutional powers. They must show that the act complained of will inflict upon them some irreparable injury. As the court below held, appellants, as public service companies, are bound by the common law, if not by statute, to render their service at reasonable rates. If the rates are not shown to be confiscatory they cannot complain that the order purporting to impose them was void, for they have suffered no injury even though the order was unauthorized."

APPELLEES' CONTENTIONS.

We have experienced difficulty in ascertaining exactly what the appellees are contending in their supplemental brief and the reasons for their contentions.

As we read their brief their contentions are:

1. That although the Commission abandoned and confessed that its second order of August 31, 1932, Exhibit M was illegal, a federal question still remained for decision by the lower court.

2. That the local rate which respondents should charge was fixed without giving the respondents their day in court.

3. That the costs of the proceeding were taxed to respondent appellees and that this was confiscation.

4. That by the Commission's order respondents would be compelled to pay 40 cents to the pipe line company and if they were required to base their rates on a 30 cent gate rate, they would not even earn operating expenses.

5. That the orders of the Commission of July 31, 1932, Exhibits L and M, although made as two orders, are in fact but one order and since the order Exhibit M is illegal—then both orders are illegal.

6. That in truth and in fact the proceedings by the Commission are a completed rate case, and the effect of the order is to confiscate appellees' property.

7. That if this Court should reverse the lower court the second order which has been confessed illegal would still be in force.

We shall discuss these contentions in their order.

1.

On page 2 of their brief, appellees state that the questions now presented are:

> "Did the court below on the allegation of the bills have jurisdiction of the case as originally instituted? If so, was such jurisdiction defeated because of some concession made during the progress of the case?"

Our answer to these questions is as follows:

The Court did have jurisdiction of the case as originally instituted insofar as it applied to the second order Exhibit M, which temporarily passed the reductions found to be proper by its first order to the local rates without first giving the appellees the right to be heard thereon, but only so far as it concerned said second order. In view of the fact that the second order was

only an interim order, when the Commission came in on the application for an interlocutory injunction and confessed that the second order was illegal and when it reiterated this statement in its answer and informed the court that it had abandoned said order because it was void, the court had jurisdiction to permanently enjoin this second order.

As to the first order we contend the court had no jurisdiction because the bills showed on their face that it was simply a preliminary order in the Commission's attempt to fix a local rate and that the appellees were not and could not be affected thereby unless and until the rate investigation started by the Commission of which the first order was a preliminary step was completed.

2.

On page 20 of their supplemental brief and at various other places the appellees contend that their local rate was fixed without notice and giving them a chance to be heard.

The claim is based upon the contention that the second or ad interim order of July 31, 1932, requiring the reduction to be passed on to the consumers until the hearing thereon fixed for October 17, 1932, is still in full force and effect. We think it is sufficient answer to this contention to call attention to the fact that the invalidity of this order Exhibit M, was confessed, and the order was abandoned, by the answer of Commission (R. 264-5). Appellants are not complaining of the in-

junction insofar as it pertains to order Exhibit M. Appellees have called attention to the fact that appellant is not complaining of the decree of the Court insofar as it permanently enjoins this order (Appellees' Sup. Brief p. 25).

It is conceded that without a hearing the Commission has no right to change or fix the local rate charged by the distributing companies.

It is true also that the Commission sustained an objection to the offer of appellees to the value and rate of return of the various units singly and collectively. But this was simply a matter of procedure, the Commission believing and holding that until the matters then under investigation which were common to all of the respondent distributing companies, to-wit: the 1¾% contract, the Gas Service Company's charge, and the gate rate, that it should not go into or hear evidence on valuations and rates of return of the 135 operating units, as the testimony as to one would not be germain to the other 134.

As was stated by counsel, during the colloquy at the hearing before the Commission, in answer to the statement of counsel for appellees, asking for a hearing for each of the distributing companies as to its valuation and financial experience.

Mr. Hatcher:

> "That is a question to take up after the Commission makes an order." (Appellees' brief, p. 169.)

After the Commission made its findings as to the contracts, common to all the distributing companies, it did made an order setting down for hearing on October 17, 1932, the question of the local rates to be charged to consumers, at which time the respondents were required to show cause and thus present any evidence as to the reasonableness of their respective local rates, from which it was intended that the Commission would determine the reasonableness of the local rates and fix them accordingly.

We submit but for the permanent injunction as to the first order, Exhibit L, that such hearings would have been held and from them such determination would now have been made—and that the only reason why appellees have not had their day in court as to their respective local rates, is because of the decree of injunction of the lower court.

3.

Appellee's contention that by its order of Aug. 31, 1932, Exhibit L, that the taxing of costs of the hearing to the distributory was confiscatory.

This claim is made by appellees on page 6 of their supplemental brief.

We do not believe that the taxing of the costs of a hearing to the utility under investigation by the Commission where it is acting within its jurisdiction, and is authorized so to do by statute, can in any sense be held to be confiscatory of its property. We know of no authority so holding.

4.

Appellees, contend, that the evidence shows that, if the distributing companies should be compelled to pay the pipe line company 40 cents and base their rates at 30 cents they could not earn even operating expenses.

This contention was made in appellees original brief and on page 4 of their supplemental brief, and is an argument going to the merits rather than jurisdiction.

We feel that we have fully answered this contention in our original brief at pages 99 to 103, to which we respectfully refer the court.

5.

Appellees contend, that the orders of the Commission of July 31, 1932, Exhibits L and M, although made as two orders are in fact but one order and since Exhibit M has been confessed to be illegal, then both orders are illegal.

This contention is made by appellees on page 9 of their supplemental brief. Counsel says:

> "If considered as one, the part of the order fixing rates was admitted by appellant to be invalid on one ground, and was found by the court to be invalid as to that ground and for the reason that it was confiscatory. This left nothing but the order Exhibit L upon which the order establishing rates was based which should have fallen and been permanently enjoined as a part of one invalid order."

Counsel are in error in their contention that the court found that the second order of August 31, 1932, Exhibit M, requiring the distributing companies effective at once to pass on the reductions on account of the Doherty

charge of 1¾% and the reduction on account of gate rate to be "passed on" to the consumers, was confiscatory. This second order was by the Commission abandoned and confessed to be invalid. Not because it was confiscatory but on other grounds and the court had no occasion to and did not find it to be confiscatory.

We are unable to see why, when in fact the Commission made two different orders, it logically follows that they must be considered but one order. The first order was complete in itself. It found as to the reasonableness of the contracts under investigation and set down for hearing and notified the distributing companies to appear on a day certain for an investigation of their local rates to consumers, as such rates might be effected by the reduction found by the Commission to be proper. The Commission claims that its first order Exhibit L was but the step in an orderly investigation of the local rates of the respondent distributing companies with the object on the part of the Commission to establish after an investigation such local rates. This order Exhibit L can be given effect without recourse to the second order and has no connection with the second order.

The second order was an ad interim order intended as is shown on its face to be in force only until the hearing provided by the first order. It was void because it attempted to put in force at once and without a hearing on that question, a reduced local rate reflecting the reductions determined by the Commission by its first order Exhibit L and was based on the erroneous assumption by the Commission that necessarily the reduction would re-

sult in a reasonable local rate which would afford the distributing companies a fair rate of return.

In order to make the first order, an investigation requiring months and great expense was necessary. The second order was without investigation, and was based on an erroneous assumption.

We submit that appellees' contention is unreasonable and the fact that the second order was void does not affect the first order and render it also void.

6.

Appellees contend that the proceedings by the Commission constitute a completed rate case, the effect of which is to constitute confiscation.

On page 24 of their supplemental brief appellees state:

> "If the proceeding before the Kansas Commission is to be considered as a completed rate case with a final order establishing rates for domestic consumers (as it must be or the final order, Exhibit "M," would not have been issued), then the court below had jurisdiction as otherwise rates would be now in effect not even producing operating expenses, the appellees would be foreclosed and estopped to question the reasonableness or legality of the thirty cent city gate rate in all future proceedings and the costs of $66,936.08 would be collected."

This statement is based on appellees' contention that the Commission has completed its investigation and has made a final order effecting the local rates. But this is contrary to the facts. Exhibit M has been confessed to be invalid and the Commission has stated in its answer

that it abandoned this order and does not intend to enforce it. At most, Exhibit M was only an ad interim order to last until the hearing which the Commission provided for on October 17. It has been enjoined with the consent of the Commission and no complaint is here made as to said injunction. Since the premises on which said contention is made are erroneous, the conclusion which appellees draw from said erroneous premises is unimportant.

7.

Appellees contend, that this Court has no authority to set aside the decree of the lower court enjoining Exhibit M or to order a dismissal of the case below.

On page 25 of its supplemental brief, appellees state:

> "The appellant did not appeal from the decree of the court below permanently enjoining that part of the orders fixing local rates (Exhibit "M"); the injunction as to that order is not before this court and in our view of the case this court has no authority at this time to set it aside or order a dismissal of the case in the court below."

The Commission has confessed that the order of Aug. 31, 1932, Exhibit M, is illegal and counsel are correct in stating that the Commission does not contend that the decree insofar as it enjoins its enforcement should not stand.

The Commission does contend that that part of the decree is invalid which enjoins the enforcement of the order of August 31, 1932, Exhibit L, wherein it found that the 40 cent gate rate charge is unreasonable and

that the distributing companies should not charge to operating expenses more than 30 cents and requiring the distributing companies to appear on a day certain and show cause why their local rates should not be adjudged accordingly and contends that the decree of the lower court, enjoining its enforcement, should be reversed, either because the District Court had no jurisdiction of the controversy insofar as it affected its order, Exhibit L, or because on the merits the order was right.

Appellees contend that when the Commission filed its answer, abandoning and confessing that its second order of August, 1931, Exhibit M, was invalid, that the court should have entered a permanent injunction and ended the case. That thereupon the case became moot because the case was there without a rate order, and that its finding and proceedings were unnecessary but that its decree enjoining the enforcement of the first order Exhibit L, as to the reasonableness of the contracts, did not become invalid and should not be set aside by this Court.

This is the substance of their contention set out on page 13 of their supplemental brief.

Appellees did not so contend in the lower court. Notwithstanding that the Commission abandoned and confessed the invalidity of the second order, Exhibit M, appellees continued to claim that by the first order their property was confiscated and by their continued prosecution of their action, after the second order, Exhibit M, went out of the case, induced the court to make findings that the cost of gas to the distributing companies

determined by the first order Exhibit M, was unreasonably low and confiscatory of their property and to enter a decree enjoining the enforcement of that order. That decree still stands, and appellant has appealed from it. We think if appellees' contention is correct, that the cause became moot when the order Exhibit M went out, then that the decree which enjoins the order of the Commission Exhibit L, should be set aside. If the question before the court was moot then it had no right to enjoin the first order as confiscatory and its decree in that respect should be set aside. On the other hand, if the question was not moot and the court had jurisdiction to enjoin the first order Exhibit L, then this Court has jurisdiction to entertain this appeal and to decide the case on the merits and review the question presented to and decided by the lower court as to whether said order Exhibit L is confiscatory of appellees' property or invades their constitutional rights, as claimed in their bill.

CONSIDERATION GIVEN INDUSTRIAL GAS.

Under the heading jurisdiction in their original brief the appellees attempt to attack the order of the Commission on the basis that it undertook to investigate the pipeline's operations as a whole and did not distinguish between the industrial and domestic business. They state:

> "So far as appears from the record and so far as any facts were developed by the said investigation, the domestic business in Kansas may have been carried on by the Cities Service Gas Company at an actual loss. The record does show that the com-

pany's industrial business was greater in extent so far as the amount of gas sold was concerned than its domestic business." (Appellees' brief, pp. 29, 30.)

Without dignifying the statement with our own denial, it is answered by appellees themselves in their attempt to justify burdening the domestic consumer with their loss of income from industrial sales.

On page 159 of their brief they state:

"The supply to industries is purely incidental and is entered into because service to domestic consumers could not otherwise be maintained. *** Therefore industrial business is not primarily sought, or kept for the purposes of profit but as a guarantee to domestic service. The price at which industrial gas is sold is determined absolutely by the price of other fuels. Before industries can be interested in the use of gas as a fuel it must be shown that they can make a saving over coal or oil, consequently without regard to profit, and even if the company was merely trading dollars, it would still be essential that the industrial business be maintained."

BUSINESS IN KANSAS.

Under the heading jurisdiction in their original brief appellees attempt to make a point of the alleged fact that most of the pipeline company's business is outside of Kansas.

On page 30 of their brief they state:

"And the investigation also disclosed that the greater part of the business of the company as a whole was done outside of the State of Kansas."

This statement if it raises any question, is disposed of

by the pipeline company's bill of complaint which states with reference to the total amount of gas sold:

> "About 58% of such gas sold was sold in Kansas and most of that which was sold to domestic consumers in Kansas was and is sold by the distributing company defendants herein." (R. 214.)

ZONING.

Under the heading jurisdiction in their original brief page 27 the companies state:

> "The Kansas Commission did not find and made no pretense of finding, the cost of supplying gas at any city gate."

This suggestion is contrary to the findings of both the court and the Commission and contrary to the evidence submitted by the companies.

One of the reasons for joining all of the companies in the investigation was to enable all of them to be present to protect their respective interests in the question of different costs at the different city gates.

No claim was made before the Commission or before the lower court that the cost at the city gates should not be the same for all the operating units. On the contrary all of the companies came before the Commission and submitted many pages of testimony contending that the gas from so many different sources was so comingled and the pipe lines were so interconnected that the cost should be the same at all cities.

On such testimony the Commission found a uniform rate as did the lower court, and the record is free of any evidence to support a contrary finding.

We believe that this suggestion now made for the first time in view of the evidence submitted is unfair both to the Commission and the court below.

CONCLUSION.

We submit in conclusion that the contentions of appellees in this controversy show a continued effort on the part of the companies to prevent a determination of the reasonableness of the payments made to the pipeline company for gas.

The decisions of the Federal Courts and the Supreme Court of the State of Kansas show a consistent effort upon the part of the Public Service Commission to investigate into the reasonableness of the payments made by the distributing companies to their affiliated pipeline company for gas. The decisions show a consistent and successful effort on the part of the pipeline company and the distributing companies to prevent such an investgiation.

The pipeline company in 1923 sought the jurisdiction of the Commission to obtain assistance because of rate controversies with the disrtributing companies none of which were then affiliated. The forty cent rate was then established because of the testimony showing a very limited supply of gas. Since that time new gas fields have been discovered which make available an almost unlimited supply of gas and the reason for the forty cent rate no longer exists. (See Record 72.)

All efforts of the Commission to investigate the reasonableness of the charge have met with technical objec-

tions not only by the pipeline company but by the distributing companies. (See Wichita Gas Co. v. Public Service Com., 126 K. 220; Wichita Gas Co. v. Public Service Commission, 3 F. Supp. 722; Western Distributing Company v. Public Service Commission, 285 U. S. 119.)

This is the only time the Commission has ever made a valuation of the pipeline company's property. Heretofore it has been precluded from such step by the claim that the pipeline was engaged in interstate commerce and that the reasonableness of its charges to its affiliated distributing plants was a matter of no concern to the Commission or at least that the authority of the Commission did not permit it to test the reasonableness of such contracts by the cost of the service rendered.

In this case the Commission for the first time has attempted to apply this test of reasonableness of the contracts under the authority of Smith v. Illinois Bell Telephone Company, 282 U. S. 133, and Western Distributing Company v. Public Service Commission of Kansas, 285 U. S. P. 119, and are again met with the same contentions.

In the case now on appeal the companies present many points of law in an attempt to have the decree of the lower court sustained without a consideration of the case on its merits. Although the only point which it pressed before the lower court was the confiscatory character of the order.

We respectfully request in conclusion that the Court guard carefully the jurisdiction of the Commission so that

it may not be prevented from proceeding to a final determination of the local rates, and we submit that if the Court finds that it has no jurisdiction of the case because of the absence of a Federal question, the decree of the lower court should be reversed insofar as it attempts to enjoin the Commission from proceeding under its order Exhibit L.

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APPENDIX.

KANSAS STATUTES.

66-107. Service, facilities, regulations and rates established by utilities. Every common carrier and public utility governed by the provisions of this act shall be required to furnish reasonably efficient and sufficient service, joint service and facilities for the use of any and all products or services rendered, furnished, supplied or produced by such public utility or common carrier and to establish just and reasonable rates, joint rates, fares, tolls, charges and exactions and to make just and reasonable rules, classifications and regulations; and every unjust, or unreasonable discriminatory or unduly preferential rule or regulation, classification, rate, joint rate, fare, toll or charge demanded, exacted or received is prohibited and hereby declared to be unlawful and void, and the public utilities commission shall have the power, after notice and hearing of the interested parties, to require any common carriers and all public utilities governed by the provisions of this act to establish and maintain just and reasonable joint rates wherever the same are reasonably necessary to be put in, in order to maintain reasonably sufficient and efficient service from such public utilities and common carriers.

66-110. Revision by commission of service, rates, regulations and practices. It shall be the duty of the commission, either upon complaint or upon its own initiative, to investigate all rates, joint rates, fares, tolls, charges and exactions, classifications or schedules of rates, or joint rates and rules and regulations, and if after full hearing and investigation the commission shall find that such rates, joint rates, fares, tolls, charges or exactions, classifications or schedules of rates or joint rates, or rules and regulations, are unjust, unreasonable, unjustly discriminatory or unduly preferential, the commission shall have power to fix and order substituted therefor such rate or rates, fares, tolls, charges, exactions, clas-

sifications or schedules of rates or joint rates and such rules and regulations as shall be just and reasonable. If upon any investigation it shall be found that any regulation, measurement, practice, act or service complained of is unjust, unreasonable, unreasonably inefficient, insufficient, unduly preferential, unjustly discriminatory, or otherwise in violation of any of the provisions of this act or of the orders of this commission, or if it be found that any service is inadequate or that any reasonable service cannot be obtained, the commission shall have power to substitute therefor such other regulations, measurements, practices, service or acts, and to make such order respecting any such charges in such regulations, measurements, practices, service or acts as shall be just and reasonable. Whenever, in the judgment of the public utilities commission shall have power to establish just and reasonable concentration, commodity, transit or other special rates, charges or privileges, but all such rates, charges and privileges shall be open to all users of a like kind of service under similar circumstances and conditions.

66-111. Investigations by commission on or without complaint. Upon a complaint in writing made against any common carrier or public utility governed by the provisions of this act, by any mercantile, agricultural or manufacturing organization or society, or by any body politic or municipal organization, or by any taxpayer, firm, corporation or association, that any of the rates or joint rates, fares, tolls, charges, rules, regulations, classifications or schedules of such public utility or common carrier are in any respect unreasonable, unfair, unjust, unjustly discriminatory or unduly preferential, or both, or that any regulation, practice or act whatsoever, affecting or relating to any service performed or to be performed by such public utility or common carrier for the public, is in any respect unreasonable, unfair, unjust, unreasonably inefficient, insufficient, unjustly discriminatory or unduly preferential, or that any service performed or to be performed by such public utility or com-

mon carrier for the public is unreasonably inadequate, inefficient, unduly insufficient or cannot be obtained, the commissioners shall proceed, with or without notice, to make such investigation as they may deem necessary. The commissioners may, upon their own motion, and without any complaint being made, proceed to make such investigation, but no order affecting such rates, joint rates, tolls, charges, rules, regulations and classifications, schedules, practices or acts complained of shall be made or entered by the commission without a formal public hearing, of which due notice shall be given by the commission to such public utility or common carrier or to such complainant or complainants, if any. Any public investigation or hearing which such commission shall have power to make or to hold may be made or held before any one or more commissioners, and all investigations, hearings, decisions and orders made by a commissioner shall be deemed and held to be the investigations, hearings, decisions and orders of the public utilities commission, when approved and filed by such commission and filed in their office, and the commission shall have power to require such public utilities and common carrier to make such improvements and do such acts as are or may be required by law to be done by such public utility or common carrier."

66-113. Orders made on hearings. If upon such hearing and investigation the rates, joint rates, fares, tolls, charges, rules, regulations, classifications, or schedules of such common carrier or public utility governed by the provisions of this act, are found to be unjust, unreasonable, unfair, unjustly discriminatory or unduly preferential, or in any wise in violation of the provisions of this act, or of any of the laws of the state of Kansas, the public utilities commission shall have the power to fix and establish, and to order substituted therefor, such rates, joint rates, fares, tolls, charges, rules, regulations, classifications or schedules as it shall find, determine or decree to be just, reasonable and necessary; and if it shall be found that any regulation, practice or act whatsoever, relating

to any service performed or to be performed by such public utility or common carrier for the public in any respect unreasonable, unjust, unfair, unreasonably inefficient, insufficient, unjustly discriminatory or unduly preferential, or otherwise in violation of any of the provisions of this act, or of any of the laws of the State of Kansas, the public utilities commission shall have full power, authority and jurisdiction to substitute therefor such other regulations, practice, service or act as they find and determine to be just, reasonable and necessary. All orders and decisions of the public utilities commission whereby any rates, joint rates, fares, tolls, charges, rules, regulations, classifications, schedules, practice or acts relating to any service performed or to be performed by such public utility or common carrier for the public are altered, changed, modified, fixed or established, shall be reduced to writing, and a copy thereof, duly certified, shall be served on the public utility or common carrier affected thereby, by registered mail; and such order and decision shall become operative and effective within thirty days after such service, and such public utility or common carrier shall, unless an action is commenced in a court of proper jurisdiction to set aside the findings, orders and decisions of said public utilities commission, or to review and correct the same, carry the provisions of said order into effect.

66-118. Action to vacate orders of commission; appeals. Any common carrier or public utility governed by the provisions of this act, or other party in interest, being dissatisfied with any order of the commission fixing any valuation, toll, rate, joint rate, fare, charge, or findings, rules or regulations, classifications, schedules, or any order or ruling fixing any regulations, practices or service, or order or ruling relating to the issuance of stocks, bonds or other securities hereinafter provided may, within thirty days from the making of such order, commence an action in a court of competent jurisdiction, against the public utilities commission as defendant, to vacate and set aside any such order, finding or decision of the public

utilities commission on the ground that the valuation, toll, rate, joint rate, fare, charges, orders, rules, regulations, findings, classifications or schedules in such decisions are unlawful or unreasonable, or that any such regulation, valuation, practice or service fixed in such order or decision is unreasonable. All actions brought under this section shall have precedence in any court, and, on motion, shall be advanced over any civil cause of a different nature pending in such court, and such action shall be tried and determined as other civil actions. Appeals from any decision of the district court shall be taken from the district court to the supreme court of the state of Kansas, in the same manner as provided by law in other civil actions. During the pendency of any action under the provisions of this act, all orders made by the public utilities commission prescribing rates, joint rates, tolls, fares, charges, rules, regulations, classifications or schedules or findings shall, unless temporarily stayed or enjoined, remain in full force and effect until final judgment is rendered therein. During the pendency of such appeal the judgment of the lower court shall remain in effect, unless stayed by order of the supreme court. Service of summons on any member of the board shall be sufficient service on the board.

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No. 114

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1933.

THE STATE CORPORATION COMMISSION FOR THE STATE OF KANSAS, HOMER HOCH, JESSE W. GREENLEAF ET AL., APPELLANTS,

VS.

THE WICHITA GAS COMPANY, HUTCHINSON GAS COMPANY, NEWTON GAS COMPANY, AND CITIES SERVICE GAS COMPANY, ET AL., APPELLEES,

BRIEF FOR APPELLEE, CITIES SERVICE GAS COMPANY.

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BRIEF FOR APPELLEE, CITIES SERVICE GAS COMPANY.

STATEMENT.

Unfortunately for this appellee, no notice of appeal nor a copy of the record was served on it by the appellant. Nor did it have any notice of, or anything to do with, the preparation of the condensed statement of the evidence presented here. It is a fact that its first knowl-

edge of these things and the first knowledge of its attorneys of record came to attention less than thirty days ago. While it is not being urged that the appeal be dismissed for this violation of the rules, it is respectfully requested that the statement as to issues be not rigidly enforced against this appellee. While we have tried to keep within the record, and we believe we have done so, yet, if the court should find any transgression it is hoped it will be viewed in the light of this statement.

Appellee, Cities Service Gas Company, is now and during all the times involved herein was, a corporation duly organized under the laws of the State of Delaware with its principal business office at the City of Bartlesville, Oklahoma, and engaged in the business of producing, purchasing, transporting and selling at wholesale natural gas in the States of Texas, Oklahoma, Kansas, Missouri and Nebraska. Its sales ranged between 100,000,000 and 330,000,000 cu. ft. of natural gas per day depending upon seasonal, economic and industrial conditions (R. 500). It was the owner of an integrated interstate gas transportation system in said states and had three main trunk supply lines, one a 20-inch line leading from the Texas Panhandle gas field, another a 24-inch and 20-inch line leading from the Oklahoma City gas field and the third a 16-inch line leading from the Seminole field of Oklahoma (R. 500). These three supply lines converged in Kansas and the gas contained therein was transported to customers in Kansas and a large portion of same was carried on to customers in the States of Nebraska and Missouri. Said appellee was the successor

to the interests of the Kansas Natural Gas Company and through a course of decisions in this court and in the state courts of Kansas, commencing with *Kansas Natural Gas Company* v. *West*, 221 U. S. 229, 55 L. Ed. 716, including *Missouri ex rel. Barrett* v. *Kansas Natural Gas Company*, 265 U. S. 298, 68 L. Ed. 1028, and ending with *Wichita Gas Company* v. *Public Service Commission*, 133 Kan. 459, it was clearly and conclusively established and decided by said courts that said business was an interstate business of such national character that it was not subject to regulation by the Commissions of Kansas or Missouri, the Kansas Supreme Court in the last-mentioned case, saying:

> "It (the record) shows that this company (Cities Service Gas Company) is an interstate one, not under the jurisdiction of the Utilities Commission, and as is well known by all who have followed the course of gas litigation in Kansas, its charges are entirely outside the power of the state to regulate."

Almost immediately after the decision of the case of *Smith* v. *Bell Telephone Company*, 282 U. S. 133, 75 L. Ed. 255, the Legislature of Kansas enacted Chapter 239 of the Kansas Session Laws of 1931, a copy of which law is annexed in the appendix hereto. Before the enactment of this statute there was no statute in Kansas in any manner relating to transactions of a public utility with an affiliate corporation. Very soon after the promulgation of said law the Public Service Commission of the State of Kansas precipitated an investigation of the contract relations between this appellee and all of its customers in the State of Kansas which were "affiliated" with

it under the provisions, definitions and descriptions in said Chapter 239 and between this appellee and Henry L. Doherty & Company, neither of which was a party to said hearing. No other customer of this appellee, whether corporate or individual, was made a party to this investigation. This appellee was neither a party to said proceeding in any stage thereof nor was there any attempt to make it a party.

The order of said Public Service Commission directing the holding of said investigation recites that,

> "The reasonableness of all contracts, and charges made by holding company to subsidiary companies of Cities Service Gas Company * * * should be inquired into for the purpose of determining the reasonableness of such contracts and the reasonableness of the charges for the services and commodities furnished."

That,

> "The contracts made and charges for services rendered and commodities furnished to said subsidiary distributing companies by the holding company and Henry L. Doherty & Company should be inquired into to determine their reasonableness and to find what amount should be allocated in this respect to the operating expense of the subsidiary companies."

and concludes with the order,

> "That an investigation be set for hearing * * * to inquire into the reasonableness of the contracts made with, and the services rendered to, the subsidiary companies of Cities Service Company by their various holding companies."

The proceeding developed into a valuation of the properties, tangible and intangible, of this appellee lying in all the states mentioned. The Commission sent its employees into all of said states and produced them as its witnesses in this hearing to show what said witnesses concluded to be the reproduction cost, depreciated, of the properties examined and considered. In this valuation the Commission accorded as the value of said properties of appellee only what it deduced from the evidence it had so produced and other evidence produced by the respondents therein as the reproduction cost, depreciated, of those portions of the properties of this appellee which said Commission was convinced should have been used by this appellee in the conduct of its said business and discarded from its valuation many millions of dollars of value of property that this appellee actually had acquired in the ordinary course of its established business and held only for the purpose of such business. The Commission determined the valuation of the properties not as they were but as they concluded they ought to be in our said business.

On August 31, 1932, said Commission as a result of said investigation and as its final order therein issued a bifurcated order, or two simultaneous orders separately signed, the substance of which was that (1) immediately effective this appellee's said customers should cease to set up upon their books any payment made to this appellee for domestic gas in excess of 30¢ per thousand cubic feet and should give no consideration to any sums so paid in excess of said price in fixing in turn their rates to their respective customers; (2) that on the next

succeeding day and continuously thereafter they pass on to their respective consumers a reduction represented by such difference in price between 40¢ per thousand cubic feet and 30¢ per thousand cubic feet. A copy of the pertinent portions of said order is set out on pages 183 and 184 of the record.

Very soon after this appellee learned of said order, it instituted its action (No. 1646-N) in the United States District Court of the proper district against the Public Service Commission, its members, the Attorney General and all of its said customers to enjoin the enforcement of said order by said officers and the obedience thereof by its said customers, alleging in its bill of complaint that the said proceeding and the said orders were illegal and that the necessary effect of same was to, and they did, contravene the rights of this appellee under the Constitution of the United States in that, *inter alia*, they deprived this appellee of its property without due process of law, impaired the obligations of its contracts, denied to it the equal protection of the laws contrary to the Fourteenth Amendment of said Constitution, and they unlawfully burdened, interfered with and regulated commerce among the states contrary to Clause 3 of Section 8 of Article I of said Constitution (R. 184-225). Upon the filing of this petition an interlocutory injunction was issued restraining said officers from the enforcement of said order and said customers from breaching their contracts with this appellee because of said order. For the convenience of the court and the parties, this action was consolidated for trial with actions No. 1637-N to and including 1645-N and they were all tried together. The

court on January 5, 1933, made findings of fact and conclusions of law and on January 28, 1933, entered its decree. The decree permanently enjoined the enforcement of the orders of said Commission, the said Commission having confessed in open court the illegality of the enforcement of the order requiring the said customers of this appellee to pass on the reduction represented by the difference between 40¢ and 30¢ in the purchase price of gas bought from this appellee, and the court having found the issues concerning all other portions of the orders in favor of this appellee. This decree is reported in 2 Fed. Supp. 792. From the decree, enjoining the enforcement of that part of the orders of the Commission concerning the price of gas, appellants have appealed.

SUMMARY OF ARGUMENT.

1. Those injured in personal or property rights will be protected against unlawful acts as well as those nominally subjected thereto.

2. Though neither a party to the hearing, nor nominally included within the order complained of, this appellee was injured by same.

3. The State of Kansas could not confer on its Public Service Commission the power to burden or regulate interstate commerce.

4. The State of Kansas did not confer the power to burden or regulate interstate commerce on the Public Service Commission; appellant.

5. The proceeding had by the Commission was *ab initio*, invalid and illegal as to this appellee.

6. The proceeding and order enjoined by the trial court were an illegal attempt to supplant the business judgment of the managing agents of the necessary customers of this appellee to its detriment, and of the managing agents of this appellee.

7. The fact of affiliation warrants a Commission in scrutinizing but does not justify penalizing.

8. Regardless of the nature of the entire proceeding of appellant Commission and of the isolated usurpations therein the Commission unlawfully eliminated and undervalued the properties of this appellee.

ARGUMENT AND AUTHORITIES.

If the decree of the court was valid, it is immaterial by what process of reasoning the conclusion was reached, and if the order of the Commission annulled by the trial court was illegal and infringed the constitutional rights of this appellee it is immaterial on what ground the said trial court found the said order of said Commission to be illegal. The question is not by what route the court or the Commission travelled but whether the destination reached was the proper one. This is trite law and hence we cite no authorities to support the assertion. Therefore we feel at liberty to approach the question in our own way and attempt to demonstrate the validity of the decree of the court and the invalidity of the orders of the Commission by the use of any valid reasons, whether or not the same were considered by said court or Commission.

1. Those injured in personal or property rights will be protected against unlawful acts as well as those nominally subjected thereto.

In determining the effect of an order affecting property rights of parties this court does not regard seriously the nominal parties subjected to the order or what the letter of the order professes to bring about but regards the consequences of the nature and necessary effects of its operation. This rule often has been laid down by this court with reference to the custom of giving the construction of the meaning of a statute by a highest

court of a given state recognition, but at the same time saying that regardless of such assigned meaning this court must form its own conclusion as to the necessary operation and effect of the statute so construed. So it has been held by this court that where a statute expressly enjoins duties upon certain persons, but in fact operates to impair the rights or injure the business or property of others that such others so injured although not mentioned nor nominally included within the terms and provisions of the law may maintain actions to restrain its enforcement. *Hill Military Academy et al.* v. *Pierce*, 268 U. S. 510, 69 L. Ed. 1070, and cases therein cited.

2. Though neither a party to the hearing nor nominally included within the order complained of this appellee was injured by same.

It is alleged by this appellee in Paragraph 16 of its bill of complaint,

> "That plaintiff's business could not be continued if it were deprived of the business of said distributing company defendants * * *" (R. 213)

and in Paragraph 16 of the answer of appellants this allegation is expressly admitted (R. 272). In the last finding of fact made by the court under Rule No. 70½ the court finds,

> "The distributing companies could not continue their business and pay the Cities Service Gas Company 40¢ per m. c. f. and predicate their rates to the consumers upon 30¢; the Cities Service Gas Company could not continue its business without the patronage of the distributing companies" (R. 319).

It was agreed by appellants that,

> "the rate established by the Commission in its order Exhibits L-H (the orders enjoined by the lower court) if applied to the business of Cities Service Gas Company for the year ending June 30, 1932, would result in a reproduction of earnings of $1,926,145.07" (R. 373).

Therefore it conclusively appears that since this appellee cannot continue its business without the patronage of said customers, that there would be an injury to it by the enforcement of the order involved to the extent of nearly $2,000,000 annually. Since it thus conclusively appears that this appellee could not continue its business without the patronage of said customers and further that said customers could not continue in business and pay this appellee 40¢ per m. c. f. for gas and charge therefor in the rate to its customers as an operating expense 30¢ per m. c. f. it inevitably follows that by this order and in this particular instance the said Commission has stricken down a contract which is an integral part of interstate business and has directly so burdened the established course of the interstate business of this appellee that it has forced upon it annually a revenue loss of nearly $2,000,000 which it would not have sustained but for such interference and regulation by a state commission.

3. The State of Kansas could not confer on said Commission the power to burden or regulate interstate commerce.

It was undisputed and expressly admitted at the trial that the business of Cities Service Gas Company was a business that was not subject to the regulation of appel-

lants. That its established course of business was and for many years past had been continuously commerce among the states could not have been successfully disputed and there was no attempt to dispute the fact, but instead, the appellants took the position that there was no attempt in said hearing or by said order to interfere with or regulate the business of this appellee. We believe that it has been sufficiently demonstrated that the order was a direct, substantial and violent attempt to burden, regulate and impair interstate commerce, practically to the extent of prostration of same. If it should be contended that the holding of a rate hearing is but an indirect and a slight burdening or regulating of interstate commerce the answer would be that no rate hearing was attempted or had. No rate or rate base was attempted to be ascertained for any distributing company customer of this appellee. The Commission instead of holding rate hearings to determine what said respective customers should charge to the public instituted only an assault upon the contracts of this appellee which fixed the price of gas bought by said distributing companies. This was entirely foreign to the functions of a public utility commission. In the case of *Nowata County Gas Company* v. *Henry Oil Company*, 269 Fed. 742, it was well said as to Oklahoma, whose laws concerning public service commission activities are well in line with the general laws prevailing over the country regarding same, and quite similar to those of Kansas, that,

> "Laws, Okl. 1913, C. 93, creating a state corporation commission, to 'have general supervision over all public utilities, with power to fix and establish rates,' etc., confers power only to fix rates to be

> charged by such utilities to their customers, and has no relation to prices to be paid by a public utility for a commodity furnished by it to the public, and the Commission is without jurisdiction over such prices, where the seller is not charged with any duty to the public."

In opinion on pages 745 and 746 this Circuit Court of the 8th Circuit, of which Kansas was then one of the component states, said:

> "Our attention has not been called to any decision by any court which holds that under the police power the state may create an administrative body or commission with authority to fix or establish prices to be paid by a public utility for things purchased and used by it, or, as in this case, for a commodity furnished by it to the public."

This case has never been reversed or disapproved and we can find no other case in any court disputing the doctrine announced.

We shall later endeavor to demonstrate the vital distinction between the act of a Commission assigning to any given element entering into the composite ultimate charge to the public, called a rate, a demonstrated reasonable value in a rate hearing, and the act of such Commission picking out any given element entering into such rate and dictating to the utility its action concerning such segregated element. The former is ordinary procedure; the latter is usurpation.

4. The State of Kansas never conferred nor attempted to confer such power on the appellant, Public Service Commission.

It will be seen that when on December 1, 1930, this court decided the case of *Smith* v. *Illinois Bell Telephone*

Company, 282 U. S. 133, this court said that in a rate hearing where the fairness of the charge of a parent or affiliate company to a subsidiary or affiliate was challenged that it was the duty of a court annulling the order of a Commission, and the duty of a Commission, to ascertain the cost of furnishing, by said affiliate to said public utility involved in such rate hearing, of the service or articles, the fairness of the price of which was so challenged. We are warranted in assuming from the sequence of events and the nature of developments that the Legislature of Kansas, when it enacted, a short time after this decision, Chapter 239 of the Session Laws of 1931, had in mind this decision and sought to carry the force of it into effect by enacting a statute concerning holding companies and affiliated corporations. It had no laws expressly dealing with or including these specific subjects. Since said chapter by ordinary rules of construction must not be considered superfluous it is fair to conclude that Kansas had no law conferring upon its Public Service Commission any power to deal with affiliated corporations in any other manner than with corporations not affiliated, and since the whole of the powers of the Commission was statutory, before the enactment of said chapter the Commission would have no power in that regard except such as would be accorded to it the same as to all other persons or entities of relying upon and enforcing the common-law rules of evidence and presumptions concerning affiliated corporations, which might be incapable, because of potential stock control, of carrying on purely adversary transactions between themselves.

This statute did not attempt to confer upon the Commission any power to scrutinize or control contracts between affiliates except those that should be made "hereafter." The contracts of Cities Service Gas Company were subsisting contracts on March 9, 1931, when said chapter took effect. It further appears that the Commission is given authority over contracts made by affiliates only,

> "in ascertaining the reasonableness of a rate or charge to be made by a public utility."

There was no rate hearing or any investigation concerning the rate or charge, of any of the distributing company customers of this appellee, pending. Finally, we must observe that the statute expressly shows what procedure shall be taken, and what the power of the Commission shall be, as to the contracts between affiliates, even as to those "hereafter" made, and in a rate hearing, when it is said:

> "Such showing shall consist of an itemized statement furnished by the utility setting out in detail the various items, cost for services rendered and material or commodity furnished by the holding or affiliated company."

We believe that the Legislature intended by this chapter to authorize only such proceedings as the Public Service Commission could constitutionally exercise and that they carefully avoided bestowing any power except in a rate hearing and that power only such as would not infringe upon the activities of an interstate instrumentality; that it was never intended that the Commission should make

a valuation of properties lying in other states or make a determination of how the business of an interstate instrumentality should be conducted. We believe that by this statute there was intended to be conferred upon the Commission only the power of ascertaining facts as they were and not the power of recasting management, policy or good faith determinations of the managing agents of a company engaged only in the conduct of interstate commerce—of for that matter of any company not so engaged.

5. The proceeding had by the Commission was, ab initio, invalid and illegal as to this appellee.

(a) It was authorized by no statute and the powers of the Commission are purely statutory. This point we deem to have been sufficiently developed as an incident to discussion of other subject matter above.

(b) The hearing was an attack upon our contracts relating to sales to public utilities and was not an attempt to determine the charges of any public utility to the public.

(c) The necessary operation and effect of the proceeding was to obstruct interstate commerce.

Without a *first sale* of our product our interstate commerce transactions could not possibly be completed. The sale is as much a part of the commerce as is the transportation or any other element of same. This has been the uninterrupted course of judicial decisions by this court from the case of *Gibbons* v. *Ogden*, 9 Wheat. 1, 6 L. Ed. 23; *Brown* v. *Maryland*, 6 L. Ed. 678, 12 Wheat. 419, to the recent case of *Dahnke-Walker Milling Company* v. *Bondurant*, 257 U. S. 282, 66 L. Ed. 239, and the very late case

of *State Tax Commission of Mississippi* v. *Interstate Natural Gas Company*, 284 U. S. 41, 76 L. Ed. 156.

(d) The proceeding violated the principles laid down in *Smith* v. *Illinois Bell Telephone Company*, 282 U. S. 133, in that it purported to ascertain the return we were making and should make from our properties in all states rather than the return we were receiving from the portions of our properties allocable to the services to the distributing companies involved or to any particular distributing company involved.

The proceeding was void on principle and as to details because the Commission did not undertake to ascertain, and made no findings upon, the cost to us of delivering the gas at the respective city gates or at any city gate. The *Smith* v. *Illinois Bell Telephone Company*, 282 U. S. 133, was reversed largely because of the same error in hearing in that case. The Commission and the court undertook to find the return to Western Electric Company from its whole business by use of all its properties and the court said that this was wrong; that the inquiry should have been as to the cost and profit ensuing from the particular transactions with the Illinois Bell Telephone Company and with it only. So in this instance we have many customers not located in Kansas, many other customers in Kansas not in any way affiliated, and it would be improper to commingle properties used in serving them and earnings received from transactions with them with those involved in serving our particular customers against whom this hearing was precipitated. In *Western Distributig Company* v. *Public Service Commission*, 285 U. S. 119, 76 L. Ed. 655, it was decided by this court that the cost or rea-

sonable charge for gas at one city gate was not even *prima facie* evidence of what the same should be at the gate of another city. We believe that this blunder of the Commission was so egregious, so fundamental and so vital, that this reason alone compels the support of the decree of the court regardless of any other impeachment of the order of said Commission.

(e) The proceeding was invalid because it fixed no rate to the consumer but undertook only to prescribe and effectually fix the rate of return of a business in interstate commerce. In view of the admissions of appellants, adverted to, that the operation of the order would entail a loss of approximately $2,000,000 annually upon us, that we could not continue our business without the patronage of our said customers and the finding of the court that our customers, the distributing company appellees, could not buy gas at 40¢ and sell it at 30¢, and the peculiar form of the proceeding and order, we believe it will become at once apparent to this court that the intention of the Commission, or at least the necessary operation and effect of its order, was that this appellee should absorb said loss and that its said sales in interstate commerce should to that extent be directly burdened by said order. This court in the said case of *Smith* v. *Illinois Bell Telephone Company*, 282 U. S. 133, forcibly remarked, when the trial court and the Commission had attempted to pass upon the fairness of a division of the revenues arising from interstate tolls, that that prerogative was lodged in the Interstate Commerce Commission and neither the court nor the Commission had any power to determine that, because it related to an interstate activity. The

thing thus denounced in the Smith case is less obnoxious than the Commission's action in this case, because in this case there was no intermixture of intrastate and interstate activities, and also for the reason that in the case of Illinois Bell Telephone Company the interstate business enjoyed the protection of the Interstate Commerce Commission, insuring it a fair rate of return, while in this case there is no commission or authority to protect this appellee except the authority of the Federal Constitution as applied by the decisions of this court.

6. The proceeding and order were an illegal attempt to supplant the business judgment of the managing agents of our necessary customers to our detriment, and of the managing agents of this appellee.

We have before stated that we should attempt to demonstrate the vital distinction between a rate hearing in which a public service commission attempts to determine and prescribe what shall be a reasonable rate for a service to the public and an attack on a contract governing the cost to the utility of only one of many elements entering into the composite quantity known as a rate. In a rate hearing a commission properly receives evidence concerning the costs of all the elements entering into operating expenses. It receives evidence concerning the fair value of the property of that utility enlisted in the service for which those rates are charged. When it has received this evidence the Commission determines in its own mind the aggregate of the operating expenses and the aggregate values of the items of property involved and determines what a reasonable return upon the value

of said property would be, and, after subtracting operating expenses from the gross return of said utility, it determines whether the net result is higher or lower than reasonable return. In the light of this information it prescribes the ultimate charge to the consumer which is called its rates. In this process it has had nothing to do with the dictating to the utility of what it shall pay to any third persons for wages, supplies, rent or any other item. If, after the fixing of the rate prescribed, the utility sees fit to recast the items of its operating activities, increasing some and diminishing others, reducing salaries, buying other or different kinds of typewriters, utilizing different stationery or in any manner changing its business policies or activities to accomplish the prescribed rate, that is of no concern whatever to the Commission. The Commission has no right to champion the cause of wage earners, of typewriter salesmen, of landlords, and by the same token has no right to assail them, so long as its prescribed rate is accomplished. If any other principle were attempted, it would mean the obliteration of corporate autonomy of all public utility corporations. If it can dictate the activity of the utility as to one purchase by it, it can of every purchase, and by whatever title it may be called every disbursement of a utility is in essence a purchase. This court has uniformly held that no public service commission can deprive a public utility of corporate autonomy and that the power of the owners of such property is the same as that of the owners of every other species of property except in these respects, that the Commission has power to prescribe reasonable rates, efficient service and to

prohibit discrimination. In *Int. Com. Comm.* v. *Chicago G. W. Ry. Co.*, 209 U. S. 108, 52 L. Ed. 705, this court said,

> "It must be remembered that railroads are the private property of their owners; that while, from the public character of the work in which they are engaged, the public has the power to prescribe rates for securing faithful and efficient service and equality between shippers and communities, yet, in no proper sense, is the public a general manager."

Again in *Int. Com. Comm.* v. *Ala. Midland R. Co.*, 168 U. S. 144, 42 L. Ed. 414, this court said,

> "Subject to the *two* leading prohibitions that their charges shall not be unjust or *unreasonable*, and that they shall not unjustly *discriminate* so as to give undue preference or disadvantage to persons or traffic similarly circumstanced, the act to regulate commerce leaves common carriers as they were at the common law—free to make special rates looking to the increase of their business, to classify their traffic, to adjust and apportion their rates so as to meet the necessities of commerce and their important interests, upon the same principles which are regarded as sound and adopted in other pursuits."

Again in *Great Western Ry. Co.* v. *Minn.*, 238 U. S. 340, 59 L. Ed. 1337, this court said,

> "A railroad's possessions are subject to its public duty; but beyond this and within charter limits, like *other owners* of private property, it may *control its own affairs.*"

This court in the case of *State ex rel. S. W. Bell Tel. Co.* v. *Comm. of Missouri*, 262 U. S. 276, 67 L. Ed. 981, said,

"Four and one-half per cent is the ordinary charge paid voluntarily by local companies of the general system. There is nothing to indicate bad faith. So far as appears, plaintiff's board of directors has exercised a proper discretion about this matter requiring business judgment. It must never be forgotten that while the state may regulate, with a view to enforcing reasonable rates and charges, it is not the owner of the property of public utility companies, and is not clothed with the general power of management incident to ownership. The applicable rule is well expressed in *Stat. Public Ut. Comm. ex rel. Springfield* v. *Springfield Gas & E. Co.*, (Ill.) 125 N. E. 891, 291 Ill. 209.

"The Commission is not the financial manager of the corporation, and it is not empowered to substitute its judgment for that of the directors of the corporations; nor can it ignore items charged by the utility as operating expenses unless there is an abuse of discretion in that regard by the corporate officers."

The proceeding and the order of the Commission are an encroachment upon and invasion of the inherent right of this appellee to conduct its interstate business in accordance with its own best business judgment.

The record discloses that the Commission in its proceedings and orders made no attempt to recognize the inherent right of this appellee to conduct an interstate business according to the best judgment of its board of directors and managing agents as they were pursuing an established business in its ordinary course and as they were conducting it at the time the hearing was commenced. The Commission instead of taking us historically as they found us sought to and did consider us as they thought our business could have been and ought to

have been conducted. They viewed our operations retrospectively and sought to recast our properties and our operations to conform with that judgment that looked backward and viewed, without responsibility for its conduct, the panorama of activities of past years that the managing agents of our company had to create while viewing the situation prospectively and had to meet as unsolved and perplexing problems, one by one, as they arose. By this method of operation this Commission lopped off from our possessions approximately 1,000,000 acres of gas leases and discarded entirely a compressor station, in Oklahoma, joined to our system which the undisputed evidence showed to be valuable as a stand-by protection for the present and as a necessary adjunct to our future operations to safely and successfully carry on our said interstate business (see affidavits of H. R. Straight, General Manager, R. 497, and of Geo. H. Baird, General Superintendent of Operations, R. 499). The said Commission also eliminated a management fee amounting to more than $50,000 annually which the proof supported (Castor's statement R. 371), although said Chapter 239 had no bearing upon a contract for such fee, since we are not a public utility under the purview of that statute, and although we were not subject to the jurisdiction of said Commission. Said Commission also eliminated many other items of operating expenses on the ground that in their business judgment they were unnecessary although all the evidence upon the point expressly dealing with such questions supported the validity of such operating expenses.

On page 498 of the record it is shown by the testimony of our general manager that we have but one single business, that of producing, buying, transporting and selling gas at wholesale in interstate commerce and derived no income except from this business. This evidence is undisputed. If this Commission could deny to us a return upon the many millions of dollars worth of property which it decided we do not need, although the evidence is undisputed that it was held only for this single business, it is a necessary result that we shall be deprived of this property. Without income to pay rentals on leases and to maintain the other properties so rejected we must sell them if we can or lose them if we can't, in obeisance to the business judgment of a political board that confessedly has no regulatory power over us but which indirectly supplants our business judgment with its judgment. If the cases cited under the last preceding heading are good law when a Commission attempts this substitution of business judgment with a regulated public utility then *a fortiori* it must be good law applied to a business in interstate commerce not subject to regulation. We confidently contend that the rule as to information to be acquired by a commission under the *Smith Case*, 282 U. S. 133, and the *Western Distributing Company Case, supra*, could by their most liberal extension be held as authority only to ascertain our business, costs and profits as they really are and could not by the most far-fetched construction contemplate a Commission torturing or remodeling our business, property or earnings into that form or extent which the Commission might fancy they ought to have.

7. The fact of affiliation warrants a commission in scrutinizing but does not justify penalizing.

The Commission in its operations upon which its order was based has made much of the fact of affiliation of our customers with us. That it regarded this element as material is demonstrated by the fact that it left out of its proceeding all of our customers that were not affiliated with us. We believe this element has a bearing only upon the *prima facie* weight of existing contracts. As between persons entirely unrelated, capable to the full extent of adversary negotiations and commitments, there is *prima facie* accorded the presumption of good faith and full value. As to persons so affiliated that, by potential stock control, the activities of each might be dominated by one superimposed entity it is possible that the law is that there is a presumption of incapacity for arms-length dealing between them and a presumption that the contract was not the result of adversary negotiations, but comprised such mutual concessions as to be beneficial to the superimposed controlling corporations. Beyond this *prima facie* aspect of the dealings, and especially in the absence existing in this case, of allegations of fraud, overreaching or imposition, we believe that a contract between related corporations is as valid as between those entirely unrelated. To epitomize the thought we assert that while affiliation justifies a commission or court to scrutinize it does not warrant them to penalize.

The form of affiliation that existed in the case of *Smith* v. *Illinois Bell Telephone Company*, 282 U. S. 133,

that existed in the case of *Houston v. S. W. Bell Tele. Co.*, 259 U. S. 318, 66 L. Ed. 961, and that existed in *State ex rel. S. W. Bell Tele. Co. v. Missouri Public Service Commission*, 262 U. S. 276, gave to American Telephone & Telegraph Company, by virtue of stock control, a much more complete power of domination of the respective utilities subject to regulation than could the form of stock control of Cities Service Company give over this appellee and over its distributing company customers. In this case Empire Gas & Fuel Company of Delaware owns the common stock of this appellee. Cities Service Company owns the common stock of Empire Gas & Fuel Company amounting to the nominal value of $37,500,000, but the public owns its preferred issue of the nominal value of $54,000,000 (R. 210, 271). Should it be assumed that beyond a certain point in the over all price for gas to the public there would be a diminishing return, or, in other words, that the traffic would bear only so large a price before return would decrease because of the lack of patronage, and that this appellee and any respective distributing company did not deal at arm's length, if there is any overreaching or imposition the natural assumption would be that it would be in behalf of the distributing companies to lower the city gate price and thus enable the distributing companies to make a larger profit than if the city gate price were higher, because Cities Service Company would indirectly receive all the profit arising from distributing company activities while the first claim upon the profits of this appellee is by law and in fact in behalf of the holders of the pre-

ferred stock of Empire Gas & Fuel Company. It is thus fair to assume that Cities Service Company would ultimately get but a portion of the profit arising from dividends upon the stock of this appellee. Condensed to its ultimate analysis the conclusion is, that any lack of arms length dealing would result not in raising the city gate price but in the lowering of it so that Cities Service Company might reap the greater and unshared profit.

Since fraud, overreaching and imposition are not alleged there only remains the question as to whether this appellee and the respective distributing company customers have sufficient corporate autonomy and activity under the evidence to prevent the respective corporate entities from being obliterated as mere instrumentalities, sham forms, simulacra. There is no evidence suggesting that such condition exists and the fact of their places of business being hundreds of miles apart and their businesses so different in character, taken with the other evidence in the case, clearly demonstrates that each corporation is moving among its fellow corporations and competitors as a separate, distinct and autonomous corporate entity, sustaining each its own liabilities, performing each its own obligations and never being called upon by anyone affiliate or stranger to assume or answer for the duties, obligations or liabilities of the other. Cities Service Gas Company is a composite of several pioneer gas corporations of Kansas and Oklahoma and aside from stock ownership in it, before alluded to, on the part of Empire Gas & Fuel Company and the further stock ownership of Cities Service Company in the latter there is no operative con-

nection between Cities Service Gas Company and Cities Service Company other than the contract that Henry L. Doherty & Company as fiscal agent of the latter when *called upon* by the former will for 1¾% of gross revenue derived from sales to unaffiliated corporations perform certain services "under the supervision of" the Board of Directors of Cities Service Gas Company. See record page 372 where this stipulation among all parties was made:

> "that there is no species of domination or control over Cities Service Gas Company * * * other than such as *necessarily* arises by ownership of all the voting stock except qualifying shares by Empire Gas & Fuel Company and as may be implied, if any, by the management contract above mentioned."

The extent to which the evidence must go to warrant courts in obliterating or ignoring corporate entity is well set out in the case of *Berkey* v. *Third Avenue Railway Co.*, 155 N. E. (N. Y.) 58. This case has been so often cited that it may well be considered to have become a leading case upon the subject. A brief excerpt from the opinion in this case is very indicative of the caution of the courts on this subject. The court said:

> "Metaphors in law are to be narrowly watched, for starting as devices to liberate thought, they often end by enslaving it. We say at times that the corporate entity will be ignored when the parent corporation operates a business through a subsidiary which is characterized as 'an alias' or 'a dummy.' All this is well enough if the picturesqueness of the epitaphs does not lead us to forget that the essential term to be defined is the act of operation. Domination may be so complete, interference so obtrusive,

that by the general rules of agency the parent will be a principal and the subsidiary an agent. Where control is less than this, we are remitted to the tests of honesty and justice."

After the foregoing generalization as to nomenclatures, metaphors and oratorical conclusions, the court sets forth concrete indicia of separate corporate life and autonomy and also in detail the things claimed to deprive it of such, which details are so pertinent to the situation here that we cannot refrain from quoting at length. The court said:

"The subsidiary deposits in its own bank account the fares collected on its route. It pays out of that account and no other the wages of the motormen and conductors engaged in the operation of its cars. It was not organized by the defendant as a decoy or blind. It was not organized, so far as the record shows, by the defendant at all. There is no evidence that at the time of its formation the defendant had any interest in it as a shareholder or otherwise. Its franchise goes back to the year 1884, and through all the intervening years it has preserved its corporate organization with property adequate to the maintenance of life. Its balance sheet for the year ending July, 1917, shows assets of $12,456,847.86. The values there stated are much in excess of the debts and liabilities, including in the reckoning of liabilities the outstanding capital stock. In no possible view, even if they are to be scaled down to some extent, are they unsubstantial or nominal. True, the subsidiary lost money that year, but so also did its parent. The fact remains that it was functioning as a corporation continuously and actively. It was so functioning at the trial in 1924. There is no evidence or suggestion that it has ceased to function since.

"The question is whether other circumstances yet to be noted neutralize these indicia of separate life and operation. The defendant, as we have seen, was the owner, in 1916, of substantially all the stock of the subsidiary corporation. Its president in reporting to the stockholders the financial situation at the end of the fiscal year informed them that to make the picture accurate, the statement must exhibit the consolidated income, and this was obviously true. Other ties must be shown in addition to the one resulting from ownership of shares. The members of the two boards of directors were nearly, though not quite, the same. Each road had the same executive officers, *i. e.*, the same president, treasurer, general manager, paymaster and counsel. The parent has made loans to the subsidiary from time to time, sometimes for construction, sometimes for operating expenses. The loan for construction expenses ($6,415,152.92) is represented by a demand note. There is nothing to show whether the money was borrowed for the original construction in 1884, or for later changes of construction when the road was electrified. The parent is also the holder of the second mortgage bonds, $1,487,000, the first mortgage bonds, however ($1,200,000), being issued to the public. The operating loans are temporary advances for electric power, for materials or supplies, and for the salaries of executive officers. As a matter of convenience, these are made in the first instance out of the treasury of the parent company. They are then charged to the account of the subsidiary, and repaid generally the following month and not later than the following year. Repayment is inconsistent with an understanding that the parent, in making the advances, was operating on its own account the cars of a connecting line. The charges are more than book entries, mere devices of an accountant. Drafts are drawn upon the subsidiary and paid with its own money. The unpaid advances for operation in July, 1917, were only $253,029.37, and this at the end of a poor year. We

are not to confuse the salaries of the executive officers with the wages of motormen and conductors. The latter, as already pointed out, were paid in the first instance, as well as ultimately, by the subsidiary itself. So were many other expenses for maintenance and repair. So were the many judgments for personal injuries recovered in the past.

"One other circumstance or group of circumstances is the subject of much emphasis in the arguments of counsel. The defendant was the dominant stockholder, not only in this subsidiary, but also in many others. The routes, when connected, cover an area from the lower part of Manhattan at the south to Yonkers and other points in Westchester at the north. All the cars, wherever used, are marked 'Third Avenue System.' On the other hand, the transfer slips bear the name in each instance of the company that issues them. The cars, when new ones become necessary, are bought by the defendant, and then leased to the subsidiaries, including, of course, the Forty-second Street Company for a daily rental which is paid. The cars leased to one road do not continue along the routes of others. The motormen and conductors do not travel beyond their respective lines. With the approval of the Public Service Commission, transfer slips are issued between one route and another, but transfers could have been required by the Commission if not voluntarily allowed. Public Service Com. Law, par. 49, subds. 3 and 6; Consol. Laws, C. 48."

On the foregoing facts it was held that the evidence was not sufficient to justify a finding of agency or the right to disregard corporate entity. This prominent case is a typical one dealing with the question of ignoring corporate entity because of affiliation by stock control and we have been unable to find any decision either of this court or any other court of precedent denying the

doctrine therein promulgated or differing with it upon essential principles involved.

In every one of the American Telephone & Telegraph cases last above mentioned this court held that the corporate entity could not be ignored and that while it justified the court to scrutinize it did not induce it to penalize. The same conclusion was reached by this court in the case of *United Fuel Gas Co.* v. *Comm. of Kentucky*, 278 U. S. 300, 73 L. Ed. 390.

Upon scrutiny of the contract and the situation of the respective parties to the gas purchase contracts we find that the undisputed evidence shows that the contract price is not higher than that of comparable unrelated corporations in the vicinity and in similar regions; that the price is not higher than that charged by this appellee to unrelated customers; that those unrelated customers are within reach of competing pipe line companies; that the 40¢ price was originally fixed by the predecessors of the Commission enjoined in this case (R. 506); there is no evidence that any city or community is complaining of this price; in short the price is the usual, current and generally accepted price for gas involving comparable transportation and dependability (see Montgomery's affidavit and schedules attached, R. 504 to 509). We contend that these elements together with the other facts in the case conclusively show that the contract price was a fair price, and no other element thereof being criticized, that, therefore, the contract itself was a fair contract. If it is a fair contract it is entitled to the same respect and weight as if it were made by unrelated corporations. This court has substantially in effect so decreed in the

American Telephone & Telegraph cases above mentioned and we know of no subsequent departure therefrom by this court.

If the contract was a fair contract it would not matter whether the price itself was somewhat above the lower limits of the price range beyond which confiscation would occur. A price may be substantially above such line of demarkation if it stays within the zone of a reasonable price. We believe that such reasonable price would be the amount that is usually and customarily arrived at by persons under similar circumstances as a result of adversary negotiations and arms' length dealing, in the absence of an overriding necessity created by a monopoly. There can be no thought of monopoly in this case under the evidence since competing pipe lines were within striking distance of our unrelated customers (see Montgomery's affidavit, R. 504 to 509). A case decided by this court clearly setting out the difference between a reasonable price and the lowest possible price before confiscation is cited in brief of appellants as authority and is *Banton* v. *Beltline Ry. Corp.*, 268 U. S. 413, 69 L. Ed. 1020. An illuminating excerpt is as follows:

> "The mere fact that a rate is not confiscatory does not indicate that it must be deemed to be just and reasonable. It is well known that rates substantially higher than the line between validity and unconstitutionality properly may be deemed to be just and reasonable, and not excessive and extortionate."

Citing *Triar* v. *Chicago Ry. Co.*, 30 Intrs. Com. Rep. 352; *Holmes & H. Co.* v. *Great Northern R. Co.*, 37 Intrs. Com.

Rep. 657; *Dimmit-Caudle-Smith Live Stock Commission Co. v. R. R. Co.*, 47 Intrs. Com. Rep. 287; *D[illegible] M. R. Co. v. Mich. R. Comm.*, 203 Fed. 864.

We confidently contend that after the *prima facie* barrier of affiliation warranting scrutiny to prevent overreaching has been hurdled by showing that the contract was the kind that was customarily made in adversary dealings and voluntarily made by those dealing at arm's length that then the distinction in law between affiliation and unaffiliation in that transaction has disappeared and that the end of the quest has been reached when it has been discovered that the contract is a fair contract. If by unusual economy, efficiency, or foresight a party to that contract has earned a per cent or fraction of a per cent more than some state commission should determine was a proper interest rate or a proper return upon an alleged "rate base," there would be no warrant in striking down the contract thus vindicated.

8. Regardless of the nature of the entire proceeding and of the isolated usurpations therein, the Commission unlawfully eliminated and undervalued our properties.

Since we were not a party to the proceeding before the Commission and since the record evidence therein produced by others was, for the mutual convenience of the court and the parties, introduced before the trial court, we necessarily have been unable to become as familiar with those proceedings and the details of the evidence so introduced as our said customers, the distributing company appellees herein. For this reason, and this alone, we adopt

the arguments and assertions by counsel for said appellees contained in their brief filed herein, relating to the merits of the appraisal actually made; that is, dealing with the amounts of the values of the respective items of our properties, whether tangible or intangible, and by reference we make said allegations and arguments a part of this brief. However, we do not confine ourselves solely in dealing with the question of the valuation of our properties to the said things so adopted and wish to call the attention of this court to the following matters:

(a) On the question of the amount and value of our gas leases we wish to call the attention of the court to the fact that they are owned by an unregulated and purely interstate instrumentality. If the Commission had been dealing, in a rate case, with a regulated company within its jurisdiction, its duty would probably have been to find what of the properties investigated were "used and useful"; but when it assumes to pass upon the value of the property of an unregulated company (assuming but not conceding that it has extraterritorial jurisdiction) it must limit its activities to the taking of such company historically as it finds it going along in its usual business, good faith assumed, of course, and value all the properties of said entity that have been bought for and are held for the business of that entity. We have shown by the testimony of our general manager (R. 498 and 499) that we engage in but one business, said witness testifying as follows:

> "That plaintiff has but one single business, which is the business of supplying gas to its patrons

through its network of pipe lines lying in the States of Texas, Oklahoma, Kansas, Nebraska and Missouri, which gas it wholesales to its customers; that it currently receives no income except that produced from said business; that unless it uses a portion of the income from said business to maintain and preserve its leasehold estates, acreages and gas reserves, same will be lost to it and plaintiff will not be able to continue in the future to have a dependable gas supply that it customarily possesses, nor give that dependable service which it has uniformly given to its patrons."

Of course, this particular piece of evidence was not before the Commission but in principle the facts were made known to the Commission. Another piece of evidence introduced before the court which would require consideration of many of the leases discarded by the Commission, even giving force to their own reasons therefor, is to be found in the testimony of our general superintendent of operations (R. 501) as follows:

"To obtain a satisfactory degree of dependability it has been necessary for plaintiff for many years past, and is now necessary for it, to have large natural gas reserves located in as diverse directions from the center of its system as is practical and with the view of preserving a dependable supply at the lowest cost, it acquired large supplies or reserves in the Seminole Field, the Oklahoma City Field, the Texas Panhandle Field, the Oklahoma Panhandle Field, the Hugoton Field, other Western Kansas fields, and Northeastern Oklahoma."

This fact was testified to by our manager and was undisputed (R. 507):

"That it is very desirable to have gas reserves located in as diverse a direction from the geographi-

cal center of plaintiff's system and markets as possible, and plaintiff's gas reserves have been acquired largely with relation to its markets and its existing or projected pipe lines and the respective capacities of such pipe lines."

It is apparent that beforehand we would be unable to divine exactly where and to what extent gas would be found underneath the ground. The effect of not obtaining prospective production acreage is shown by our said general superintendent of operations (R. 503) as follows:

> "That if plaintiff should wait for the discovery and development of new fields by others it would probably frequently experience shortages of supplies necessary for its markets while so waiting for others to take the lead, and also if plaintiff should abjure all initiative on its part and wait for others to develop gas fields it would be compelled to pay exorbitant prices for its gas reserves and supplies and at times be confronted with the alternative of either paying prohibitive prices or being short of gas."

The propriety of dealing in a different way with an unregulated interstate company from that which would be proper with a regulated utility becomes apparent if we consider underlying reasons. A commission may well restrict a regulated utility to the possession of properties that are only presently or in the immediate future "used and useful" on the ground that its customers should not pay for benefits to accrue very far in the future. This can be done safely because the regulated utility theoretically is continuously assured of a reasonable return upon the properties it may have at any given time by the power and duty of the Commission to so regulate its rates as to currently produce that reasonable

return. We as an unregulated interstate entity can have and claim no such protection and, therefore, we must prudently prepare our affairs, so far as careful foresight will enable, so as to protect ourselves against vanishing gas fields, economic vicissitudes and other future menacing problems. If we wait while others lead and have to pay exorbitant prices there is no one to mend our fortunes. We must fight our own economic battles and of necessity must use the judgment of our managing agents to meet our problems.

The court found that the cost of our gas leases was something over $5,000,000 but found that the fair value of them was about $12,000,000 (R. 313). There is a margin of approximately $7,000,000 there which under the authority of the case of *Los Angeles Gas & Elec. Corp.*, 77 L. Ed. ...., 820 of Advance Sheet No. 13 of Reports covering the 1932 term of this court, should be taken by this court for our benefit if this court should consider that the trial court considered any other item of value more advantageously to us than the law would warrant. In *United Fuel Gas Co.* v. *Comm. of Ken.*, 278 U. S. 300, 73 L. Ed. 390, this court said the Commission and trial court were authorized to take the cost only because no better standard or yardstick of value was presented. We confidently contend that the Commission materially erred in appraising our leases at approximately $3,000,000 because it saw fit to exclude practically a million acres of leases which it claimed were not "used and useful" and that we have a margin to spare as to those values above the allowance by the trial court of approximately $7,000,000 worthy of the consideration of this court.

(b) The Commission excluded from its valuation a large compressor station attached to the southeastern portion of our pipe line system, in Oklahoma, because it was not presently "used and useful" in that it was not being operated. Our evidence (which was produced before the trial court, but not before the Commission because we were not a party) showed,

> "That on account of extensions into Missouri and the said consequent enlargements plaintiff has been, and is holding the Hogshooter Compressor Station in constant readiness to serve its said pipe line system and especially its said extensions into Missouri. That by use of said compressor station it would add a transmission capacity of approximately 20,000,000 cu. ft. of natural gas daily and by such use it can accomplish such result much cheaper than in any other manner. That while said order of the said Texas Railroad Commission is operative it will be necessary for plaintiff in cold weather to use said Hogshooter Compressor Station to increase the transmission capacity of its lines from whatsoever source it gets its added supplies, and whether said Texas order remains in force or not upon resumption of normal financial conditions or the natural growth of more markets along the said newly constructed extensions, the economical operation of plaintiff's system will require the operation of the Hogshooter Compressor Station" (R. 504).

We believe it is not possible even under the theory of "used and useful" limitations to discard Hogshooter Compressor Station under this evidence, which was undisputed, and that while under the *Los Angeles Gas & Elec. Decision*, 77 L. Ed. . . . , it might be proper to reduce its value below what would obtain if it were used every day, as the court evidently did, yet there can be no possible dis-

pute of its value as a "stand by" resource and we contend the Commission erred in excluding it and that the trial court was right in including it at its demonstrated fair value.

(c) The Commission excluded the payment of 1 3/4% of gross sales to unaffiliated corporations paid by us to Henry L. Doherty & Company as fiscal agents of Cities Service Company for services. The court in reaching its decree failed to allow anything for this item, saying that, while a portion of the amount involved was evidently proved yet the proof was not clear as to the precise amount to be allowed (R. 299 and 300). If we are right in our contention that the Commission must take our activities as they find them and do not have the power to restrict, in the absence of the charge of fraud or lack of good faith, then we were entitled to have the payments which we actually made under this contract credited to us as operating expense. This amount for the year 1932 was more than $50,000 and for preceding years considered by the Commission was considerably above that amount. Since the net return was approximately 1 15 of the value of assets the rejecting of this item of operating expense would be equivalent to deducting about $700,000 from the base on which they figured a return. We believe that we are entitled to the consideration of this elimination when the court under the doctrine of the *Los Angeles Gas & Elec. Case*, 77 L. Ed. , seeks to determine whether any material error has been committed in the decree of the court enjoining the order of the Commission.

(d) The Commission disallowed as operating expenses the annual payments we were making on non-producing leases in order to prevent their forfeiture. This reduction of operating expenses, automatically increasing alleged rate of earnings, amounted to more than $300,000 for the year of 1932 (R. 314). For the same reasons herein advanced supporting our right to own all the property which we actually in good faith had and held for this single business we were entitled to this allowance and the order of the Commission denying it was invalid. Since such disallowance would be equivalent to striking from the alleged rate base approximately $5,000,000 the item would go far in and of itself to show the confiscatory character of the order of the Commission.

(e) In denying to us any allowance for dry hole expense other than a parsimonious allowance for one dry hole a year the Commission vouchsafed to us infinitely more wisdom in the ascertainment of where gas would be found thousands of feet under the ground than it accorded to us in the general management of our affairs. During the test year more than $170,000 was expended by us on dry holes. A denial of this sum for operating expenses annually would be equivalent to a reduction of the alleged rate base by more than $2,000,000 and it will easily be seen that, where the rate fixed by the Commission is confessedly close to the line of confiscation, or as we claim already below it, this item itself would likely put it well below that line.

We leave the other errors of the Commission involving more complicated details to the brief of other appellees entirely because of our lack of opportunity as aforesaid of possessing the same degree of familiarity with those things as those have who were involved in the proceedings before the Commission.

We respectfully submit that in view of the record in this case and the law applicable thereto that this court should affirm the judgment and decree of the court below.

JAMES W. FINLEY,
Bartlesville, Oklahoma,
R. E. CULLISON,
Bartlesville, Oklahoma,
Counsel for Appellee, Cities Service Gas Co.

APPENDIX.

Chapter 239—Kansas Laws 1931.

PUBLIC SERVICE COMMISSION JURISDICTION IN RELATION TO HOLDING COMPANIES.

Senate Bill No. 304.

An Act relating to the public service commission, in relation to holding companies and of transactions between affiliated interests and public utility companies.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF KANSAS:

Section 1. (1) The public service commission shall have jurisdiction over holders of the voting capital stock of all public utility companies under the jurisdiction of the commission to such extent as may be necessary to enable the commission to require the disclosure of the identity in respective interests of every owner of any substantial interest in such voting capital stocks. One per centum or more is a substantial interest, within the meaning of this subdivision.

(2) Such commission shall have jurisdiction over affiliated interests having transactions, other than ownership of stock and receipt of dividends thereon, with utility corporations and other utility companies under the jurisdiction of the commission, to the extent of access to all accounts and records of such affiliated interests relating to such transactions, including access to accounts and records of joint or general expenses, any portion of which may be

applicable to such transactions; and to the extent of authority to require such reports to be submitted by such affiliated interests, as the commission may prescribe. For the purpose of this section only, "affiliated interests" include the following:

(a) Every corporation and person owning or holding directly or indirectly ten per centum or more of the voting capital stock of such utility corporation.

(b) Every corporation and person in any chain of successive ownership of ten per centum or more of voting capital stock.

(c) Every corporation ten per centum or more of whose voting capital stock is owned by any person or corporation owning ten per centum or more of the voting capital stock of such utility corporation or by any person or corporation in any such chain of successive ownership of ten per centum or more of voting capital stock.

(d) Every person who is an officer or director of such utility corporation or of any corporation in any chain of successive ownership of ten per centum or more of voting capital stock.

(e) Every corporation which has one or more officers or one or more directors in common with such utility corporation.

(f) Every corporation which the commission may determine as a matter of facts, after investigation and hearing, is actually exercising any substantial influence over the policies and actions of such utility corporation even though such influence is not based upon stockholding,

stockholders, directors or officers to the extent specified in this section.

(g) Every person or corporation who or which the commission may determine as a matter of fact, after investigation and hearing, is actually exercising such substantial influence over the policies and actions of such utility corporation in conjunction with one or more other corporations and/or persons with which or whom they are related by ownership and/or blood relationship or by action in concert that together they are affiliated with such utility corporation within the meaning of this section even though no one of them alone is so affiliated: Provided, however, That no such person or corporation shall be considered as affiliated within the meaning of this section, if such person or corporation is otherwise subject to the jurisdiction of the commission or such person or corporation shall not have had transactions or dealings other than the holding of stock and the receipt of dividends thereon with such utility corporation during the two-year period next preceding: Provided further, No foreign holding company shall acquire the stock or control of a local operating unit or public utility in its own name or through a trustee without first entering into an agreement to keep the public service commission fully informed as to the transactions between the subsidiary or local operating unit and the holding company, and to submit to the jurisdiction of the commission in so far as such transactions affect the rate or charge to be made by the subsidiary or local operating unit.

Sec. 2. No management, construction, engineering or similar contract, hereafter made, with any affiliated interest, as hereinbefore defined, shall be effective, unless it shall first have been filed with the commission. If it be found that any such contract is not in the public interest, the commission, after investigation and a hearing, is hereby authorized to disapprove such contract.

Sec. 3. In ascertaining the reasonableness of a rate or charge to be made by a public utility, no charge for services rendered by a holding or affiliated company, or charge for material or commodity furnished or purchased from a holding or affiliated company, shall be given consideration in determining a reasonable rate or charge unless there be a showing made by the utility affected by the rate or charge as to the actual cost to the holding or affiliated company furnishing such service and material or commodity. Such showing shall consist of an itemized statement furnished by the utility setting out in detail the various items, cost for services rendered and material or commodity furnished by the holding or affiliated company.

Sec. 4. This act shall take effect and be in force from and after its publication in the official state paper.

Approved March 6, 1931.

Published in official state paper March 9, 1931.

FILE COPY

NOV 15 193

In the

Supreme Court of the United States

October Term, 1933.

No. 114.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, and JESSE W. GREENLEAF, THURMAN HILL, and C. W. CAMPBELL, as members of said COMMISSION OF KANSAS, and HOMER HOCH, JESSE W. GREENLEAF and ERNEST E. BLINCOE, as members, substituted, and ROLAND BOYNTON, Attorney General of the State of Kansas, *Appellants*,

vs.

THE WICHITA GAS COMPANY, a Corporation, *Appellee*.

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vs.

THE WESTERN DISTRIBUTING COMPANY, a Corporation, *Appellee*.

THE PUBLIC SERVICE COMMISSION OF THE STATE OF KANSAS, *et al.*, *Appellants*,

vs.

CITIES SERVICE GAS COMPANY, *Appellee*.

(Reported below 2 Fed. Supp. 792.)

BRIEF FOR APPELLEES

other than Cities Service Gas Company.

SMITH-GRIEVES, LAW PRINTERS, KANSAS CITY, MO.

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(Reported below 2 Fed. Supp. 792.)

BRIEF FOR APPELLEES

other than Cities Service Gas Company.

PRELIMINARY STATEMENT.

The controversy herein involves two orders of the Public Service Commission of Kansas entered the 31st day of August, 1932, in proceedings held under the authority of Chapter 239 of the Session Laws of Kansas of 1931. The pertinent provisions of this statute are as follows:

Under Section 1, the Public Service Commission of the State is given jurisdiction over the holders of the voting capital stock of public utility companies, and access to all accounts and records of affiliated companies; and the Section sets out various definitions with respect to the powers granted and the utilities and affiliated interests affected by the statute.

Section 2 provides that no management, construction, engineering or similar contract made after the enactment of the statute with any affiliated interest shall be effective until filed with the Commission.

Section 3, which is the only section under which the proceedings had and complained of herein could be said to have been authorized is as follows:

> "In ascertaining the reasonableness of a rate or charge to be made by a public utility, no charge for services rendered by a holding or affiliated company, or charge for material or commodity furnished or purchased from a holding or affiliated company, shall be given consideration in determining a reasonable rate or charge unless there be a showing made by the utility affected by the rate or charge as to the actual cost to the holding or affiliated company furnishing such service and material or commodity. Such showing shall consist of an itemized statement furnished by the utility setting out in detail the

various items, cost for services rendered and material or commodity furnished by the holding or affiliated company."

The statute above quoted became effective March 9th, 1931; and on July 2nd, 1931, the then Public Service Commission of the State of Kansas issued an order which is attached to the Bill of Complaint herein, as Exhibit "A," in its docket number 13127, entitled "In the Matter of the Investigation of the Reasonableness of Contracts, and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company." (R. 25.)

Under the provisions of this order, three separate and distinct contracts were listed for investigation as follows:

1. The contract under which the several distributing companies in Kansas, being all of the Appellees herein other than the Cities Service Gas Company, paid to the Cities Service Gas Company for gas for domestic purposes approximately the sum of forty cents (40c) per thousand cubic feet at their respective city gates.

2. Payments made to The Gas Service Company for services rendered, by it to the several distributing companies, appellees herein.

3. Payments made to Henry L. Doherty & Company by the several appellees in the sum equal to 1¾% of their gross revenues in return for services rendered by said Henry L. Doherty & Company.

The Public Service Commission of Kansas and the court below found that the payments made by the several distributing companies to The Gas Service Company were proper and approved the same, and no appeal has been

taken by any of the Appellees from the decision of the court below with respect to its ruling as to the contract with Henry L. Doherty & Company, so that this proceeding involves only the right of the Kansas Commission to investigate and determine in the manner undertaken by it, the reasonableness of the forty cent (40c) city gate rate paid by the several distributing companies, Appellees herein, to the Cities Service Gas Company, an affiliated company.

The reasonableness of this forty cent (40c) city gate rate was litigated in proceedings brought by the City of Wichita, and its reasonableness was upheld by the Supreme Court of Kansas in a decision rendered June 9, 1928, in the case of *The Wichita Gas Company* v. *The Public Service Commission,* 126 Ks. 220; 268 Pacific 111, that company being one of the Appellees herein.

The reasonableness of this rate was again upheld by the United States District Court for the District of Kansas in the subsequent case of *The Wichita Gas Company* v. *The Public Service Commission,* decided May 28, 1930, and reported in 3 Fed. Sup. 722.

Within a very few months after the decision last cited was rendered, the Kansas Public Service Commission called for hearing the application of The Western Distributing Company for an increase in rates in the city of El Dorado, that company contending that it was not at the time making its operating expenses. In the course of that proceeding and notwithstanding the two prior decisions as to the reasonableness of the forty cent (40c) city gate rate, the Commission required the applicant to again make a showing as to the reasonableness of that rate. The applicant contended that the cost would be prohibitive, introduced the two prior decisions, and refused to make a further showing. The

application for an increase in rates was thereupon dismissed; and The Western Distributing Company took its case to a three-judge court in the District of Kansas, and from an adverse decision appealed to this Court which affirmed the decision of the lower court as reported in the case of *The Western Distributing Company* v. *The Public Service Commission,* 285 U. S. 119.

When this proceeding instituted by the Kansas Public Service Commission on its own motion was called for hearing (R. 25), the several distributing companies, Appellees herein, entered their special appearance objecting to the jurisdiction of the Commission as set out in Exhibit "B" (R. 27) to the Bill of Complaint herein. When the case came on for trial before the court below, Plaintiff waived the objection previously raised, set out in Exhibit "B" to the Bill of Complaint, that it was improperly joined with other distributing companies.

The Appellee distributing companies do, however, contend that in the proceeding ordered and held by the Kansas Commission there was no issue of a rate or charge to be made by a public utility, and that said Commission was not acting "in ascertaining the reasonableness of a rate or a charge to be made by a public utility," as is provided by the statute, which is the source of its authority to act.

In the proceeding before said Commission, it was repeatedly contended by the Commission and its attorneys that the proceeding did not involve the investigation of the rates charged by said distributing companies (the Appellees herein other than the Cities Service Gas Company), to their consumers in the respective cities served by them, and no opportunity was given to said distributing companies to show the value of their property or their experience under existing rates; and such oppor-

tunity, when repeatedly demanded, was expressly refused by said Commission. (R. 28, 44, 47, 51, 67, 371.)

In the several Bills of Complaint filed by the Appellee distributing companies respectively, the following allegations were made and proven without contradiction in the court below:

THE WICHITA GAS COMPANY. That the value of its property used and useful in rendering service to its consumers in the city of Wichita, Kansas, was $2,872,854; that its gross earnings for the year ending June 30th, 1932, were $1,818,850; that its net earnings applicable to depreciation and return for said period were $181,096; and that if certain salary reductions had been in effect during said entire period, its net earnings would have been $205,434.00, or an earning of only 7.2% for all purposes of depreciation and return on the present fair value of its property.

THE HUTCHINSON GAS COMPANY. That the present fair value of its property used and useful in rendering service to its consumers in the city of Hutchinson, Kansas, was $584,169; its gross earnings for the year ending June 30th, 1932, were $426,678; and that as a result of its operations for the year ending June 30th, 1932, it failed in the sum of $36,146 to make its operating expenses.

THE NEWTON GAS COMPANY. That the present fair value of its property used and useful in rendering service to its consumers in the city of Newton, Kansas, was $284,865; its gross earnings for the year ending June 30th, 1932, were $173,076; and that as a result of its operations for the year ending June 30th, 1932, it failed in the sum of $10,496 to make its operating expenses.

THE PITTSBURG GAS COMPANY. That the present fair value of its property used and useful in rendering service to its consumers in the city of Pittsburg, Kansas, was $379,772.00; its gross earnings for the year ending June 30th, 1932, were $153,297; that its net earnings applicable to depreciation and return for said period were $21,414; which, if adjusted to present conditions for salary reductions would have been $24,499 or an earning of only 6.5% for all purposes of depreciation and return on the present fair value of its property.

THE CAPITAL GAS & ELECTRIC COMPANY. That the present fair value of its property used and useful in rendering service to its consumers in the city of Kansas City, was $3,398,092; that its gross earnings for the year ending June 30th, 1932, were $1,143,299; that its net earnings properly adjusted for salary reductions during that period would have been $160,495, or an earning of 4.7% for all purposes of depreciation and return on the present fair value of its property.

THE WYANDOTTE COUNTY GAS COMPANY. That the present fair value of its property used and useful in rendering service to its consmers in the city of Kansas City, Kansas, was $3,769,687; that its gross earnings for the year ending June 30th, 1932, were $1,687,706; that its net earnings for said period after proper adjustment for salary reductions would have been $253,995 or a return of only 6.7% for all purposes of depreciation and return on the present fair value of its property.

THE GIRARD GAS COMPANY. That the present fair value of its property used and useful in rendering service to its consumers in the city of Girard, Kansas, was $46,545; that its gross earnings for the year ending June 30th,

1932, were $16,770; that its net earnings for said period after proper adjustments for salary reductions would have been $1,953 or an earning of 4.2% for all purposes of depreciation and return on the present fair value of its property.

UNION PUBLIC SERVICE COMPANY. That the present fair value of its property used and useful in rendering service to its consumers in the fifty-one (51) towns served by it was $2,779,839; that its gross earnings for the year ending June 30th, 1932, were $1,073,081; that its net earnings for said period after proper adjustments for salary reductions would have been $106,291 or an earning of 3.8% for all purposes of depreciation and return on the present fair value of its property.

THE WESTERN DISTRIBUTING COMPANY. That the present fair value of its property used and useful in rendering service to its consumers in the twenty-seven (27) towns served by it was $769,703; that its gross earnings for the year ending June 30th, 1932, were $408,656; that its net earnings after proper adjustments for salary reductions would have been $15,926 or an earning of only 2.1% for all purposes of depreciation and return on the present fair value of its property.

THE ARKANSAS VALLEY GAS COMPANY. That the present fair value of its property used and useful in rendering service to its consumers in the city of Arkansas City, Kansas, was $440,772.00; that its gross earnings for the year ending June 30, 1932, were $190,985.00; that its net earnings after proper adjustments for salary reductions would have been $27,262.00, or an earning of only 6.2% for all purposes of depreciation and return on the present fair value of its property.

ALL DISTRIBUTING COMPANIES. That the present fair value of their properties in the aggregate used and useful in rendering service to their consumers in all of said cities was $15,326,298; that their gross earnings for the year ending June 30th, 1932, were $7,092,398; that their net earnings for the year ending June 30th, 1932, after proper adjustments for salary reductions would have been $756,989 or an earning of only 4.9% for all purposes of depreciation and return on the present fair value of the properties of all said distributing companies.

The Cities Service Gas Company, which furnishes the supply of gas to all the Appellee distributing companies, was not a party to the proceedings had before the Kansas Public Service Commission, the Commission admitting at all times that it had no power, jurisdiction or authority to fix rates to be charged by that company in its interstate business. Nevertheless, the Commission employed expert engineers who undertook to make a valuation of all property belonging to the Cities Service Gas Company, although the greater part of such property was outside the State of Kansas and beyond the jurisdiction of the Commission; and also employed expert accountants who went to the office of the Cities Service Gas Company at Bartlesville, Oklahoma, outside the jurisdiction of the Commission, to audit its books. These engineers and accountants testified before the Commission as to their respective findings.

The several distributing companies, Appellees herein, showed to the Commission that they respectively had been notified by the Cities Service Gas Company that gas could not and would not be furnished to them for less rates than those at the time being charged, and the distributing companies took the position before said

Commission and before the Court below that as none of them at the time was making proper or adequate returns its would be impossible to survive if they were required to pay 40c per thousand cubic feet for gas at their respective city gates, and base their rates to consumers on a price of 30c per thousand cubic feet, and if they were required so to do their property would be confiscated. In order to avoid this situation, the distributing companies undertook to show the reasonableness of their respective contracts and introduced detailed and voluminous evidence as to value of the property of the Cities Service Gas Company and its experience under the existing contract.

As a result of these proceedings, the Commission on July 20, 1932, issued its order (R. 69) directing that the several distributing companies cease to set up on their books as an expense item any payment for gas at the city gate in excess of 29.5 cents per M. C. F., and

> "That on and after the 1st day of August, 1932, the rate to the consumer shall be reduced by the distributing companies in proportion to the reduction in expenses above named, pending a final determination of the distributing company rates. Such reductions to be measured by the ten-cent reduction per M. C. F. and 1¾ per cent of the gross revenue of the distributing companies."

Following the application of the several distributing companies for a rehearing, said Commission set aside the order of July 20, 1932, and on August 31, 1932, issued two orders attached to the several Bills of Complaint herein as Exhibit "L" (R. 59) and Exhibit "M" (R. 62).

Exhibit "L" contains an order in practically the same language as above quoted from the order of July 20, 1932, except that the city gate rate is fixed at 30c instead of 29½c (R. 59).

In Exhibit "M" it was ordered "that effective September 1, 1932, and until a hearing is held and an order issued, that the distributing companies, respondents above named, shall charge rates to the consumers as follows:

"All distributing companies paying a gate rate in excess of 30 cents per M. C. F. shall deduct the difference between what the distributing company is now paying at the city gate and 30 cents per M. C. F. and pass on this difference to the consumer" (R. 62).

In the court below it was admitted by counsel for the Commission that order Exhibit "M" directing the distributing companies to pass on to their respective consumers the difference between the expense of purchasing gas at any rate in excess of 30c per M. C. F. and 30c was invalid, and the Commission consented to a permanent injunction as to that order, so that the order Exhibit "M" is not now in issue herein (R. 282).

It is apparent, however, that the order Exhibit "M" was void for reasons other than those admitted by the Commission. The order undertook to reduce local rates immediately, and then later—we have reason to believe, much later—determine whether such reduction was justified. The fact that the companies might suffer confiscation in the meantime was either ignored or intended. It would seem that the Commission purposely refused to hear evidence as to the local rates intending to immediately put into effect reduced rates, the reasonableness of which it would later consider.

SUMMARY OF ARGUMENT.

1. In the absence of a proceeding the purpose of which was to ascertain the reasonableness of a local rate to consumers, the Commission had no jurisdiction in this proceeding.

2. The issue presented to this court is moot for the reason that in the absence of an inquiry as to proper local rates the question as to what was the value of the property of the Cities Service Gas Company or its earnings as of a past date is merely a matter of curiosity.

If the above propositions are not adopted:

3. The earnings of the Cities Service Gas Company on its last available experience, June 30, 1932, are reasonable on the valuation founded by the Commission, particularly under the statutes of the State of Kansas cited.

4. In determining the reasonableness of the contract under consideration, such determination should be based on present values and present experience, and not on average values and earnings.

5. The findings of the court below as to the value of the property of the Cities Service Gas Company are supported by the overwhelming weight of evidence, and should be increased rather than decreased.

Jurisdiction.

We have made the foregoing preliminary statement in order to enable this court better to understand the issue, if any, now before it for determination.

It was admitted below, and doubtless will be admitted here, that the Commission has no power or jurisdiction

to establish rates to be charged by the Cities Service Gas Company in inter-state commerce. The repeated decisions of this court holding that no such power or jurisdiction exists are set out in the opinion of the court below, and a re-citation of them here is not necessary.

It was also admitted in the court below, and doubtless will be admitted here, that the Kansas Commission was not undertaking in the proceedings had by it to determine reasonable rates to be charged by distributing companies to their respective customers; that no valuation was made by said Commission of any of said distributing company properties, or any investigation made to determine whether or not the rates then being charged by said distributing companies respectively were adequate.

There was no evidence as to any of these matters before the Commission, and in the court below the only evidence was that of the Appellee distributing companies showing the value of their respective properties and their operating experience as alleged in the several Bills of Complaint and as stated in the foregoing Preliminary Statement. This uncontradicted evidence shows that the distributing companies as a whole were, under existing rates, earning only 4.9% for all purposes of depreciation and return on the then fair value of their properties in the aggregate.

The Commission refused to hear any of this evidence as to the value of the properties of the several distributing companies or their operating experience; but, nevertheless, without any knowledge whatever of the situation, undertook by Exhibit "M" to direct that all rates be reduced as of September 1, 1932. (R. 62.)

That both the refusal to hear evidence and the establishment of rates pending future investigation are beyond the power of the Commission was held in the very recent

case of *Rockland Light & Power Company* v. *Milo R. Maltbie et al.*, reported in 148 Miss. 22, and decided by the New York Supreme Court, Albany County, June 9, 1933. In that case the court said:

> "It would appear that by the exclusion of certain testimony and exhibits offered by petitioner the Commission committed prejudicial error in that such excluded testimony and exhibits established prima facie that the said temporary rates prescribed by the Commission would yield a return of less than 4 per cent on the value of petitioner's property used and useful in the public service. The exclusion of this evidence for the reason stated in the decision of the hearing commissioner, which was adopted by the Commission and embodied in its order, in itself, warrants the suspension of the order directing the establishment of temporary rates until the matter may be determined on the merits.
>
> The Commission cannot disregard all rules of procedure and deny to a petitioner the privilege of introducing evidence in a rate case as to the value of its property. In the discharge of its duty a fair hearing is a fundamental requirement, and where rights depend on facts a finding without giving consideration to available material evidence is an arbitrary exercise of power inconsistent with rational justice. *Interstate Commerce Commission* v. *Louisville & N. R. Co.*, (1913) 227 U. S. 88, 57 L. ed. 431, 33 S. Ct. 185."

No order has been issued since August 31, 1932, and no attempt of any kind has been made since that date to change or modify the rates of the distributing companies in any respect.

There is no application or proceeding of any kind pending before said Commission at this time by any city served by any of the Appellee distributing com-

panies or by the Commission on its own motion to determine any of such rates; and no attempt has been or is being made by said Commission to ascertain the value of the property of any of the distributing companies or to determine the reasonableness of their respective earnings under existing rates.

It is our contention that in this proceeding there is no justiciable issue before this Court, and that the only question presented is the right of the Kansas Commission to determine in the manner undertaken by it the moot question as to what a proper city gate rate was as of September 1st, 1931.

As above stated, the reasonableness of said city gate rate has been twice determined in connection with the ascertainment of proper rates to be charged by the Wichita Gas Company to its consumers in the city of Wichita, one determination having been made by the Supreme Court of the State of Kansas in 1928, and the other by the District Court of the United States for the District of Kansas, First Division, in 1930.

In the Western Distributing Company case, this Court held that the determination of a proper city gate rate for the city of Wichita was not even prima facie evidence as to the reasonableness of a rate to be charged at El Dorado, Kansas, some thirty (30) miles distant. The Kansas Commission prevailed in the Western Distributing Company case on the ground that the adjudication of a reasonable gate rate for one city had no bearing on the reasonableness of the gate rate in a city thirty (30) miles distant. It is at least inconsistent on the part of the Commission thereafter to enter upon an extended investigation on its own motion and at the conclusion thereof to establish a uniform gate rate applicable to all cities in Kansas, notwithstanding the fact that gas must be

transported two hundred seventy (270) miles farther to supply some cities than others. Especially is this true when it established this uniform rate without any evidence as to any of the other operating costs of any distributing company, without consideration of the valuation of any distributing company's property or its gross and net income, and in disregard of all other considerations upon which the decision in the Western Distributing Company case was based.

The Commission now contends that 30c is a reasonable rate to be charged at the city gate of every city in Kansas served by the pipe line system, although it contended in the Western Distributing Company case that an adjudication as to the gate rate at Wichita had no bearing on the gate rate at El Dorado.

This proceeding is so unusual that the citation of precedents is impossible. So far as we are aware, no like proceeding has ever been undertaken by any commission anywhere. What the Commission did, was to undertake to determine the value of the property of the Cities Service Gas Company over which it admittedly had no control, and to determine its operating experience and earnings as an abstract proposition unrelated to any inquiry then or since pending before it as to the reasonableness of local rates to be charged by any company. The item of purchased gas is one of the hundreds of items entering into the operating expense of every distributing company selling natural gas. The cost paid for coal or other fuel by any utility manufacturing gas or by any utility manufacturing electric energy is also a major item of expense in the operations of all such utilities. We do not believe, however, that it would be contended that any Commission without having before it some proceeding involving rates to be charged the public would have the

right to establish the price of any such fuel and attempt to hold the several utilities to that price in the future when the question of their rates might be under investigation.

A somewhat similar situation was before the Supreme Court of Missouri in the case of *State ex rel. Columbia Telephone Company* v. *Atkinson et al.*, — Mo. — 195 S. W. 741. In that case the Missouri Commission had before it the question of rates to be charged by the telephone company at Columbia, Missouri. The Commission found for the company so far as rates were concerned, but fixed the value of the company's property at a figure which the company considered unreasonably inadequate. An appeal was taken and the Court held that if rates were not involved, the question as to what the value of the property might be was moot. The Court said:

> "The only purpose of ascertaining the value, as mentioned in the complaint in No. 282, was to find out whether the rates were reasonable and to secure a reduction of rates. While the statute, authorizing the commission to ascertain the value of the property of such companies, stands by itself as a separate provision of the Public Service Commission Act, we cannot see that the Commission would be required, as a mere matter of curiosity independent of any purpose it might serve, to go to the labor and expense of ascertaining the value of any such property. Such action, when taken by the commission, is for some definite purpose; usually for the purpose of fixing rates, although it might be done when the commission has before it for consideration the propriety of allowing the issuance of stocks and bonds, or of any other acts of a corporation over which the commission has supervision."

The same question was again before the Supreme Court of Missouri in the case of *West St. Louis Water & Light Co.* v. *Public Service Commission of State of Missouri,* 197 S. W. 340, the facts and decision of the Court being thus stated in the syllabus:

> "Certain residents of the county where defendant water and light company operates its plant filed with the Public Service Commission complaints as to rates, etc. The Commission proceeded to ascertain the value of appellant's plant, and found that the rates, except in minor details, were not unreasonable. The company brought the matter for review to the circuit court, complaining only of the findings as to valuation. The order of the Commission was upheld, and the case appealed. Held, that the question of valuation was a moot question, and would not be reviewed."

We concede that under the decision of this Court in the case of *Smith* v. *Illinois Bell Telephone Company,* 282 U. S. 133, the Kansas Commission in determining proper rates to be charged by any of the several distributing companies to their consumers could require a showing as to the reasonableness of the price paid for gas to an affiliated company, the clear purpose of that decision being to enable such a commission to ascertain whether the earnings of the distributing company and the affiliated supply company when considered together and the whole treated for rate making purposes as a common enterprise were unreasonable. That, however, is not this case. The Commission was admittedly not undertaking to fix rates for distributing companies and repeatedly refused to permit any evidence to be introduced as to the value of their properties or their operating

or any other facts (see this brief page 5) upon which an intelligent determination of rates could be based.

The legislature of Kansas by Chapter 239 of the Session Laws of 1931 had this same thought in mind when it enlarged the powers of the State Commission, for the power so granted is expressly limited for use "in ascertaining the reasonableness of a rate or charge to be made by a public utility."

The utter futility of any such proceeding is clearly apparent in view of the present economic experience in the United States. The National Recovery Act has required the Cities Service Gas Company and all the distributing companies to adopt codes, and such codes have been adopted and signed. Operating expenses have been materially increased thereby. This fact does not appear in the record, but as stated by this Court in the case of *Atchison, Topeka & Santa Fe Railroad Company et al.* v. *United States et al.*, 284 U. S. 248:

> "There can be no question as to the change in conditions upon which the new hearing was asked. Of that change we may take judicial notice. It is the outstanding contemporary fact, dominating thought and action throughout the country."

It is likewise a matter of common knowledge that the thought and effort of the present administration has been devoted largely to increasing commodity prices, and it is a matter of common knowledge of which this Court may take judicial notice that such prices have materially increased. The property of the Cities Service Gas Company consists largely of pipe, compressor stations and buildings. The commodities out of which these several units have been constructed have all increased and so have labor costs, and to say that they will not further

increase in the future is to say that the efforts of the present administration are to result in failure.

What, then, is the present purpose of determining what the value of the property of the Cities Service Gas Company was as of September 1, 1931, or what its earnings were at that time? There is no rate case pending, and no valuations have been made by the Commission of any distributing company property. It would be not a matter of months but a matter of years to make the required valuations and audits and to properly present the same before the Commission. When that time arrives, if it ever does, of what value then will be the determination of the Commission as to the value of the property of the Cities Service Gas Company and its earnings as of September 1, 1931? If the determination of the reasonableness of the 40c city gate rate at Wichita in 1928 and in May, 1930, was not even prima facie evidence as to the reasonableness of the city gate rate at El Dorado thirty (30) miles from Wichita four (4) months after the decree of the District Court of the United States for the District of Kansas, of what possible value could the determination of the Kansas Commission as to a reasonable gate rate in 1931 be in proceedings which may or may not be brought in future years as to reasonable local ratees to be charged by other and more distant distributing companies?

We have set out in detail in our preliminary statement the separate and aggregate values of the properties of the several distributing companies (as of September, 1931, now much higher), and their several and aggregate earnings. The Commission and the court below have found the value of the property of the Cities Service Gas Company and its earnings. These several facts taken together constitute the "over-all" picture and show conclusively

that when the properties are considered as a whole for rate making purposes, the "over-all" earning is inadequate.

As above stated, we believe this proceeding to be without precedent. We also believe that the Commission in issuing the two orders of August 31st, 1932, was not acting in good faith. From argument made to the court below, we believe its purpose was, to fix a low rate which the distributing companies would be in the future permitted to pay the pipe line company and charge to their respective operating expenses, but to so frame the order that neither the pipe line company nor the distributing companies could say that their property was being confiscated, and so that none could appeal or in any manner invoke the jurisdiction of any court to review the Commission's action. Its intention was, that this order should become final by reason of not being subject to review, and that in future cases, it would be used as a starting point without regard to the then existing conditions. This contention was thus disposed of by the court below:

> "If the construction of counsel for the Commission is correct, the order is plainly an attempt to avoid a judicial review in this court of the matters therein determined, and to deprive the distributing companies of their constitutional rights. This cannot be tolerated."

In the two cases above cited where the 40c city gate rate was found to be reasonable by the Supreme Court of Kansas and the District Court of the United States, the Commission and the respective courts had before them proceedings properly instituted to determine reasonable rates to be charged by the Wichita Gas Company to consumers served by it. In both of these cases, the reason-

ableness of the city gate rate became material solely by reason of the fact that local rates were properly under investigation, and in both of those cases, the Wichita Gas Company recognizing the right of the Commission to such information voluntarily assumed the burden of proving the reasonableness of such city gate rate.

In the Western Distributing Company case the proceeding was again a proper one authorized by statute, being the application of the Western Distribution Company for the determination of reasonable rates to be charged by it to its consumers in the city of El Dorado. In that case, the Commission had its engineers make a valuation of the property used and useful in rendering service to consumers in El Dorado, the company did likewise, and a full showing was made as to all matters necessary to the determination of a reasonable rate to be charged local consumers. As above stated, the Court held the adjudication in those cases was not prima facie evidence for use in determining the rates for any other city; but it certainly did not hold in the Western Distributing Company case, or in any other case, that the Kansas Commission, or any other commission, having before it no inquiry as to rates could determine as an abstract proposition the reasonableness of one item of the operating costs of any public utility, especially when such determination was as to the price of a commodity transported and sold in interstate commerce.

In this proceeding, the Kansas Commission consistently refused to admit any testimony as to the value of the property of the several distributing companies, and consistently refused to listen to any evidence as to their earnings. This attitude was maintained in the court below where the Commission objected to the distributing companies introducing any evidence as to the value of

their respective properties or their operating experience on the ground that the Commission had had no opportunity to investigate any such matters or to value the property of the several distributing companies and on the further ground that such matters were not in issue until the Commission had made an investigation for the purpose of determining the fair value of the properties owned by the distributing companies and their rate of return. It was stipulated in the court below as follows:

> "It is further stipulated that the witness F. C. Hamilton will testify that he is familiar with the value and fianancial experience of the distributing companies, plaintiffs herein, and that the value of their respective properties and their operating experience is as set out in the several bills of complaint of the complainants herein other than the Cities Service Gas Company, to which the Public Service Commission objects on the ground that the testimony is irrelevant, incompetent and immaterial, and further states that it has had no opportunity to investigate this matter or value the property and that it was the intention of the Commission to do so in pursuance of its order set out in plaintiff's bill of complaint of Exhibit 'L.' (R. 371.) (Exhibit 'L' was confessed to be void before this objection was made.)
>
> "It is further stipulated that the witness F. C. Hamilton will testify that if the several distributing companies complainants herein are compelled to pay the price they are now paying the Cities Service Gas Company for gas at their respective city gates and are compelled to base their rates to consumers upon the price fixed by order, Exhibit 'M,' they will not be able to make operating expenses, with nothing for return and depreciation on the value of their property, to which testimony the Commission objects on the ground of incompetency, the subject matter not coming in issue until the Commis-

sion has made an investigation for the purpose of determining the fair value of the properties owned by the distributing companies and their rate of return." (R. 371.)

In the foregoing discussion we have endeavored to point out two propositions in a sense separate but at the same time so related that a discussion of one involves the other. These propositions are:

First, the Commission not having acted "in ascertaining the reasonableness of a rate or charge to be made by a public utility," the proceeding is not authorized by the Kansas statute or the decisions of this Court.

Second, rates to consumers not being involved, the determination of the abstract question as to what was a proper price to pay for gas at the city gate at a given past date without applying such finding in any manner is merely the determination of a moot question.

The above discussion has proceeded on the theory that the Commission, as it repeatedly stated, never intended to ascertain local rates. This theory and these repeated statements are borne out by such actions of the Commission as the joining of companies operating in one hundred thirty-five (135) cities and communities in one proceeding where they could not possibly present separate rate cases; the failure to make valuations, audits or other investigation as to any of the distributing companies; the refusal to permit any of the distributing companies to introduce any evidence as to such matters before it, and the objection to any such evidence in the court below.

Why two orders were issued instead of one on August 31, 1932, we can only surmise. By all proper practice, one order only should have been issued, as was done July 20, 1932, and the two orders should now be con-

sidered as one. They were handed down simultaneously in decision of the same proceeding. The two taken together constitute a finding and a judgment. The judgment has been abandoned and set aside, leaving only the finding. Even if the two orders taken together did concern local rates, the order now in controversy does not. It is not, in fact, an order at all; it is a finding as to a moot question. The only semblance of an order is the direction that the several distributing companies cease to set up on their books any amount paid for purchased gas in excess of 30c, and the further suggestion that they *should* not consider a greater amount in fixing local rates. As to bookkeeping, if the books are to mean anything at all, they must set up an actual transaction, and as to rates, the companies are not fixing them; they are already fixed, and can only be changed by the Commission as provided by law, which law requires not only a full hearing and investigation but an express finding that existing rates are unjust and unreasonable.

The Kansas Commission neither made the required investigation, nor made any finding as to the unreasonableness of existing rates. These failures alone entitled the appellees below to a permanent injunction against the order of the Kansas Commission and all parts of it, as was held by Chief Justice Taft in the case of *Wichita Railroad & Light Company* v. *Public Utilities Commission of the State of Kansas*, 260 U. S. 48, from which we quote the following from page 58:

> "The proceeding we are considering is governed by Sec. 13. That is the general section of the act comprehensively describing the duty of the Commission, vesting it with power to fix and order substituted new rates for existing rates. The power is expressly made to depend on the condition that after

> full hearing and investigation the Commission shall find existing rates to be unjust, unreasonable, unjustly discriminatory or unduly preferential. We conclude that a valid order of the Commission under the act must contain a finding of fact after hearing and investigation, upon which the order is founded, and that for lack of such finding the order in this case was void."

In that case there was an order without any finding; in this case there are findings without any order.

In the brief for appellant it is stated, "The Commission assumed jurisdiction under the authority expressed in the recent case of *The Western Distributing Company* v. *The Public Service Commission of Kansas*, 285 U. S. 119." This is rather remarkable as that case was decided February 23, 1932, over seven months after the proceeding of the Kansas Commission was instituted.

Elsewhere in the brief is cited the case of *Smith* v. *Illinois Bell Telephone Company*, 282 U. S. 133.

We can find nothing in either of these cases supporting this assumed jurisdiction.

In the Western Distributing Company case, the local distributing company was asking an increase in rates. All this Court held in that case was that before being entitled to such relief, the company should have complied with the Commission's demand that a showing be made as to the *cost* of supplying gas at the city gate.

In the Illinois Bell Telephone case, this Court expressly disapproved the exact thing which the Kansas Commission did in the case at bar instead of authorizing it as claimed by the appellant. In that case the court below found the earnings of the Western Electric Company over a period of years, and found them to be reasonable. This Court remanded the case for findings

as to the *cost* of the service rendered the Illinois Bell Telephone Company as distinguished from the cost of all business done by the Western Electric Company.

The Kansas Commission did not find, and made no pretense of finding, the cost of supplying gas at any city gate. It merely found the aggregate earnings of the Cities Service Gas Company from all classes of business, industrial (not regulated) and domestic, and in Missouri, Oklahoma, and Texas as well as Kansas. There is certainly nothing in either the Western Distributing Company or the Illinois Bell Telephone Company cases authorizing any such thing, and the authority granted by the Kansas statute is expressly limited to the ascertainment of "actual cost."

The court below clearly had jurisdiction in the several suits brought by the appellees herein, for it had before it a complete order in two parts, one part finding a rate, the other applying the finding to local rates. The orders taken together require the distributing companies to put in effect rates to local consumers based on a price for purchased gas 10c a thousand cubic feet less than the price for which it could be purchased. These local rates were put into effect by the Commission without any investigation whatever as to local conditions and after refusing the distributing companies opportunity to be heard with respect to them. The undisputed evidence in the court below, as shown by the stipulation above quoted, was, that such rates would not permit the distributing companies to earn even their operating expenses, and they were clearly confiscatory. (R. 371.) Therefore, the court below had jurisdiction. This jurisdiction was admitted by the Commission when it confessed the invalidity of the order establishing local rates and consented to a

permanent injunction as to it. This confessed injunction should have ended the litigation and carried with it a permanent injunction as to all other parts of the order whether contained in one instrument or in two.

The situation here presented is somewhat similar to that in the case of *United States* v. *Los Angeles R. R.*, 273 U. S. 299, where the Interstate Commerce Commission made a final report on value (called an order) but made no order respecting rates. Suit was brought to enjoin and annul this order, but this court held that the order differed essentially from all those held by the court to be subject to judicial review, and said:

> "Each of the orders so reviewed was an exercise either of the *quasi*-judicial function of determining controversies or of the delegated legislative function of rate making and rule making. The so-called order here complained of is one which does not command the carrier to do, or to refrain from doing, any thing; which does not grant or withhold any authority, privilege or license; which does not extend or abridge any power or facility; which does not subject the carrier to any liability, civil or criminal; which does not change the carrier's existing or future status or condition; which does not determine any right or obligation. This so-called order is merely the formal record of conclusions reached after a study of data collected in the course of extensive research conducted by the Commission, through its employees. It is the exercise solely of the function of investigation. Compare *Smith* v. *Interstate Commerce Commission*, 245 U. S. 33. Moreover, the investigation made was not a step in a pending proceeding in which an order of the character of those held to be judicially reviewable could be entered later."

So here, what remained of the orders of August 31, 1932, after that part of the order fixing rates was confessed to be void, became nothing more than a voluntary and unauthorized excursion of the Commission into intercompany contracts which might very properly be a part of a rate proceeding, but should not be used as a means of precluding inquiry into the same evidence whenever such a rate hearing might be had.

Upon the confession made by counsel that the order, (Exhibit "M," R. 62) was void the court below should have entered a permanent injunction without hearing any evidence in the case, because the remaining issues were moot.

Even though we may be carrying this argument to the extent of being tedious, we again insist that there is nothing in either the Western Distributing Company or the Illinois Bell Telephone Company case which authorizes the Kansas Commission to attempt indirectly to fix a gate rate for the Cities Service Gas Company to be applied to its inter-state business. This is exactly what the Commission undertook to do. It did not confine its investigation to Kansas or even pretend to ascertain the cost to the Cities Service Gas Company of supplying gas to the city gate of any city in Kansas; but on the contrary, undertook to investigate its operations as a whole in every state in which it does business, and including all kinds of business transacted by it. The Kansas investigation concerned only domestic rates in Kansas. That investigation did not and could not have had anything to do with any other kind of business or with the business in any other state. So far as appears from the record and so far as any facts were developed by the said investigation, the domestic business in Kansas

may have been carried on by the Cities Service Gas Company at an actual loss. The record does show that the company's industrial business was greater in extent so far as the amount of gas sold was concerned than its domestic business. And the investigation also disclosed that the greater part of the business of the company as a whole was done outside of the state of Kansas. If the Kansas procedure was proper and authorized by the decisions of this Court as claimed, so would a like procedure be proper in Missouri, Oklahoma, or Texas. The confusion which would result from any such independent investigations by independent commissions is readily apparent. It cannot be assumed that any of the other states would find the same values or that they would come to the same conclusion as to the earnings of the company, especially if such other commissions should consider their investigation as limited to gas sold for domestic purposes instead of to all business transacted by the company, or should limit their investigation to a determination of the earnings of the company from domestic business in their particular state.

We submit that the proceeding had before the Kansas Commission was not authorized by statute or by the decisions of this Court; that all parts of the two orders should have been permanently enjoined, and that the decree of the court below should be affirmed for the reasons stated.

Jurisdiction on the Admitted Facts.

In our previous discussion we have endeavored to show that the Kansas Commission had no authority under statute or decision to undertake the investigation which it did undertake. Under this heading it is our purpose

to show that said Commission, on the facts found by it, and assuming for the purpose of argument that such findings are correct, had no authority to enter the order which it did enter, if any part of said order is now the subject of adjudication.

The value of the property of the Cities Service Gas Company as found by the Commission was $73,170,510.00 as of September 1, 1931. (R. 53.)

In its brief at page 147, appellant admits that this figure is not correct, due to the fact that the Commission depreciated overheads but made no allowance in annual reserves to take care of such depreciation. The amount which appellant admits should be added to the Commission's valuation is $1,011,392.00, which makes the value of the property as of September 1, 1931, $74,181,902.00.

Assuming for the purpose of argument that this finding of value is correct, it is our contention that if it was proper for the Kansas Commission to investigate the over all earnings of the Cities Service Gas Company from all classes of business in all states in which it transacts business, that even in such event the earnings found by the Commission for the last available period were reasonable earnings on the valuation so found and that the Commission and the court below should have so found and eliminated from the present consideration the necessity of a detailed and laborious examination of the correctness of the Commission's findings as to value.

The Commission found the earnings of the Cities Service Gas Company for the year ending June 30, 1932, to be $7,963,813; that replacement reserves for said period should be $1,977,591; and that the net income of the company after reserves applicable to return on the value of said property was $5,986,222. (R. 55.) This earning is a return of 8.07 per cent on the value of the

property of the Cities Service Gas Company as above recited.

In arriving at the above earnings, the Commission disallowed an item of operating expense amounting to $52,297.13 representing payments made to Henry L. Doherty & Company by the Cities Service Gas Company under the one and three-quarters per cent contract, and $50,000.00 charged as expense to amortize the cost of the proceeding before the Commission. It is contended by appellees that these deductions should not have been made for the reason that the Commission has no power of regulation over the inter-state business of the Cities Service Gas Company, and no power to disapprove the contract between it and Henry L. Doherty & Company. If this Court finds these deductions should not have been made, the net earnings of the Cities Service Gas Company become $7,861,516.00, and the net income after admitted reserves becomes $5,883,925.00 or 7.93 per cent of the value as found by the Commission.

We do not desire to be understood as agreeing to the figure of $5,883,925 as representing the actual or correct net income of the Cities Service Gas Company for the year ending June 30, 1932. In arriving at that net figure, the Commission made its own arbitrary allowances for depreciation, depletion, amortization, and dry hole expense in the sum of $1,977,591, which appellees contend is entirely inadequate. These allowances were made on average requirements over a period of years and had nothing whatever to do with the then situation or with the future. We are merely assuming these figures as correct for the purpose of argument, and are referring to them as facts admitted by the Commission.

On these admitted facts, the question is presented to this Court as to whether an earning of seven one-

hundredths of one per cent over 8 per cent is such an earning as can in any sense be considered unreasonable in view of the hazardous business in which the pipe line company is engaged.

The court below in discussing the jurisdiction of the Commission approached the subject from two angles. The first view expressed was, that the distributing companies and the pipe line company were, in effect, one common enterprise, and that *in determining local rates,* the Commission had the right to determine a reasonable return to the Cities Service Gas Company for producing, transporting and delivering gas at the respective city gates of the cities served. The second view expressed was, that if the Commission had authority only to scrutinize and inquire into the reasonableness of contracts between affiliated companies, the same result would necessarily follow and that the only way in which the reasonableness of such contracts could be determined was to ascertain the reasonableness of the return to the Cities Service Gas Company on its property used and useful in its business. (R. 286.)

It is our contention that a return of either 8.07 per cent or 7.93 per cent is reasonable.

We do not believe there is a better definition as to what constitutes a reasonable rate than that given by the court below in its supplemental opinion. This definition is as follows:

> "A 'reasonable rate' is not a particular decimal. A 'reasonable rate' is one that falls within the zone of reason; it is a field and not a mathematical point. The lower limit of the zone of reason is confiscation, that is, denial of a net return sufficient to preserve property and attract capital necessary to enable the utility to discharge its public duties. A finding that

> a particular rate is reasonable is not, therefore, a finding that every other rate is either unreasonable or confiscatory." (R. 320.)

As we understand the decision in the Western Distributing Company case, the appellees herein would not be required in any proper proceeding before the Kansas Commission to make any showing as to the reasonableness of the price paid by them for gas purchased if such purchase was from a company not affiliated with them. The sole and only reason for the requirement of such showing is, that the companies are affiliated. In the Western Distributing Company case, this Court said:

> "It is enough to say that, in view of the relations of the parties and the power implicit therein arbitrarily to fix and maintain costs as respects the distributing company which do not represent the true value of the service rendered, the state authority is entitled to a fair showing of the reasonableness of such costs, although this may involve a presentation of evidence, which would not be required in the case of parties dealing at arms' length and in the general and open market, subject to the usual safeguards of bargaining and competition."

If a reasonable rate is a zone and not a decimal point, and if the only reason for requiring a showing as to the reasonableness of such rate is the fact of affiliation, the question as we look at it then becomes a question of whether or not a court can say as a matter of law that a return of 8.07 per cent or a return of 7.93 per cent is without the zone of reason and such a rate of return as unaffiliated companies dealing at arms' length would not countenance.

If such a rate of return is within the zone of reason and such as an unaffiliated company engaged in the hazardous business of producing and transporting gas should reasonably expect, then there is no need of further discussion of the issue, if any, now presented.

In the court below all of the witnesses for appellees testified that 8 per cent was a minimum reasonable rate of return; and the only witness for the Commission (who qualified only by reason of being a former member thereof) testified that in normal times 8 per cent would be a proper rate of return, but that present times were abnormal, meaning thereby that capital under existing conditions could not be procured for an enterprise limited to such a rate of return.

The court below found in its finding number XVIII that 8 per cent was not unreasonable, such finding being as follows:

> "A return of approximately 8 per cent upon present values is necessary, under present conditions, to assure confidence in the financial soundness of the Cities Service Gas Company, to maintain its credit, and to enable it to raise money necessary for the discharge of its public duties. Any return substantially lower than that would be confiscatory. *United Railways* v. *West*, 280 U. S. 234, 252.
>
> *Rate of Return.* The pipe line company is subject to the hazards attendant upon the production of gas, and its transportation to distant markets. The amount of gas it may take from its own wells, and the price it may charge for its product, is subject to regulation by public authority. It must find a market in a highly competitive field. It competes with coal and fuel oil in household heating and for industrial purposes; the competition of fuel oil is particularly formidable for house-

hold heating; improved oil burners are automatic, approved by the National Board of Fire Underwriters for safety, are as clean as gas, and dependable. Electricity has absorbed the household lighting and is making serious inroads on cooking. In short, it must search for and find its gas; transport it hundreds of miles without an hour's interruption; then find and satisfy its customers. The law contemplates that it make no more than a fair return in good times; it should not be forced to take less when times are hard. There is evidence that in years past the profits of the company exceeded 10 per cent. We do not analyze those figures; in rate making, the past must bury its dead; a confiscatory rate cannot be ordered for the future because an exorbitant profit was made in the past. *Georgia Ry.* v. *R. R. Comm.*, 262 U. S. 625, 632; *Board of Commrs.* v. *N. Y. Tel. Co.*, 271 U. S. 23, 32.

What is a proper return is a question of fact in which the elements of time and place play an important part. In this part of the Middle West, it is a recognized fact that in normal times, public utilities must promise a return of approximately 8 per cent, if capital for construction and extensions is to be attracted from other investments. The Kansas statutes recognize 8 per cent as a minimum return for a waterworks property (Sec. 13-1201, R. S. Kan. 1923) and provide for a recapture of a portion of the earnings over 10 per cent of gas and electric companies (Sec. 13-1204, *id.*). The Kansas Supreme Court has held that earnings from 8 to 9 per cent on telephone properties are reasonable. *The State ex rel.* v. *Telephone Co.*, 115 Kan. 236. The witness for the Commission testified that 8 per cent would not be an unreasonable return in normal times, but testified that these times are abnormal, as they are. But if abnormality is considered, the return must be increased, not decreased. In these times, when stock of the best

utilities can be purchased on a 9 per cent basis or better, certainly an 8 per cent return on this hazardous enterprise is not unreasonable." (R. 317.)

The evidence upon which the above finding of the Court was based was that of F. C. Hamilton, a member of the executive committee of Henry L. Doherty & Company and in charge of the rate and valuation department of that company; P. McDonald Biddison, a gas engineer of national reputation, who testified that he had had many years' experience in financing gas properties; and Charles F. Clark, associated with Halsey, Stuart & Company of Chicago, who testified that he had spent practically his entire business life in intimate touch with financial operations of the largest industries of the United States. All of these witnesses testified that under existing economic conditions a fair return should be in excess of 8 per cent, that neither at this time nor in the immediate future could it be hoped that capital could be attracted to a project such as that of the Cities Service Gas Company for a return of 8 per cent, but that a much greater return would be required if capital could be interested at all. (R. 528.)

The only evidence for the Commission was that of C. H. Montgomery, an expert accountant employed by the Commission and a former member thereof, who testified as follows:

"Q. You stated in your judgment 8 per cent was the amount in normal times that would interest capital? A. A maximum of 8 per cent in normal times.

Q. Are times very abnormal now? A. They are, very, at this time.

Q. Do you think you could interest capital in a project of this sort at 10 per cent now? A. It might

be difficult to interest capital under any conditions right at this time.

Q. Wouldn't you say, then, that under present conditions 8 per cent would be the minimum? A. If this project was being initiated at this time, it would be difficult. If such a proposition would be initiated under these conditions, it would be difficult to secure capital at a reasonable amount, if it was contemplated that these conditions would continue for an indefinite length of time.

Q. Well, suppose we are reproducing this property as of September 1, 1931. Was the condition at that time any different than what it is now? Was the condition any different on September 1st, the date we have chosen for this reproduction, than it is now? A. That would depend. Any change in condition probably has been for the worse.

Q. These financial experts have been seeing rainbows in the sky, have they not? A. They are still seeing them in the future, but conditions have probably become worse since September 1st.

Q. Well, what do you say? Is 8 per cent as of September 1, 1931, an unreasonable rate of return? A. If it was contemplated that those conditions would last indefinitely and if in view of those conditions anyone would have the courage to go out and embark on such an enterprise, they would probably expect to receive a higher rate than 8 per cent. * * *"

The Kansas Supreme Court in the case of *The Wichita Gas Company* v. *Public Service Commission,* 126 K. 220, 268 P. 111, in construing the Kansas public utility law and the authority of the Kansas Commission held that the question of a proper rate of return was a question of fact to be determined according to the evidence adduced, and said:

"The proposed question is one of fact, to be determined according to those standards by consideration of evidence duly produced at the trial of the issue. The evidence will include estimates and opinion evidence, and will involve an element of prophecy; but the finding of the court in a rate review case, based on the evidence, of fair compensation for public utility service, is a finding of fact. To the extent a rate does not fairly compensate the utility for its service, it is unjust, unreasonable, and unlawful, within the meaning of the Public Utilities Act (Rev. St. 1923, 66-101 to 66-195). A rate may also be confiscatory, and hence unlawful, on constitutional grounds. But a rate may be enjoined as unjust and unreasonable which is not so low as to be confiscatory of property. *Railroad Co.* v. *Utilities Commission*, 95 Kan. 604, 148 P. 667. The finding of the referee was that 8 per cent was not merely a fair return, but was necessary for a fair return."

The finding of the court below as set out in finding number XVIII above quoted is the only finding that could have been made on the evidence adduced before the Commission and the court; and if a proper rate of return is to be determined on the evidence, such finding should not be disputed.

If, then, 8 per cent on the undisputed evidence is a reasonable rate of return, does it follow that a return of 8.07 per cent or 7.93 per cent is beyond the zone? If a variation of seven one-hundredths of a per cent is sufficient to take a rate out of the zone of reasonableness, then certainly reasonableness means but a decimal point and not a zone; and if 8 per cent is the minimum reasonable rate, as all witnesses testified and as the court below found, then, clearly, 7.93 per cent is reasonable, and the court below should have found for the plaintiffs

and should have permanently enjoined the orders of the Commission without concerning itself further with the Commission's valuation, and this court should now on the admitted facts affirm the lower court without further examination of the valuation.

In the foregoing discussion as to what constitutes a reasonable rate of return, we have considered the matter from the viewpoint of testimony of witnesses before the Commission and general legal principles which should be applicable to a proceeding such as this. If, however, there remains any doubt, such doubt should be overcome by the Kansas statutes which clearly express the views of the Legislature as to what constitutes a reasonable return, and prohibit certain cities from fixing rates to be charged by a gas utility which will not produce an earning of *at least 8 per cent.* We quote the following from Chapter 14, Article 17, being Section 14-1701 of the Revised Statutes of Kansas 1923:

> "The board of commissioners of any such city, at all times during the existence of such contract, grant, privilege or franchise, shall have the right by ordinance to fix a reasonable schedule of maximum rates, and to make reasonable changes therein from time to time, to be charged such city and the inhabitants thereof for gas, light and heat, electric light, power or heat, or steam heat, and the rates of fare on any street railway, and the rates of any telephone company, or the rates charged any such city or the inhabitants thereof by any person, firm or corporation operating under any other franchise under this act; and the board of commissioners, under the provisions of this act, shall have the right to change or modify any such schedule of rates, after giving due notice and granting a hearing to the interested parties of their intention so to do: *Provided further, however,* that said boards of commissioners

shall at no time fix a rate which shall prohibit such person, firm or corporation from earning at least eight per cent on the amount of its actual cash investment in such city over and above its reasonable operating expenses and the expense for maintenance and taxes."

It will be observed from the language of this statute that it was not the intention of the Legislature to limit the rate to 8 per cent and its sole purpose is to prohibit cities from establishing a rate which will not produce *at least* that rate of return.

The above quotation is from the section of the statute applying to cities of the second class. The statute with respect to cities of the first class is even more favorable to appellees and clearly shows the intention of the Legislature to permit utilities operating in cities of the first class to earn a return of *at least 10 per cent.* Section 13-1204 of the statutes contains provisions with respect to the consideration which a city of the first class is to receive for franchises granted, and gives such city the right to fix rates to be charged by utilities supplying gas and electricity and contains this provision:

> "*Provided, however,* that said governing body shall at no time fix a rate which will prohibit such person, company or corporation from earning at least 10 per cent on its capital invested in such city over and above its reasonable operating expenses and the expenses for maintenance and taxes."

There has never at any time during the course of this proceeding been any evidence presented to the Commission or to the court below which indicated that under present rates the Cities Service Gas Company was earning either 8 or 10 per cent on its invested capital or on

the present value of its property. And on the admitted facts as herein set out, the order of the Commission should have been enjoined by the court below and the decision of that court should now be affirmed.

The Supreme Court of Kansas in the case of *The Wichita Gas Company* v. *Public Service Commission*, 126 K. 220, 268 Pac. 111, and the United States District Court for the District of Kansas in the case of *Wichita Gas Company* v. *Public Service Commission*, 2 Fed. Supp. 792, have each held that an 8 per cent return was proper for a gas distribution system with respect to which there was no element of mining hazard, such as we have herein pointed out as existing in the case of a company engaged in the production and transportation of natural gas.

Considering the nature of this investigation, the fact that the rates to local consumers were not involved, and that the only purpose was to determine the reasonableness of an existing contract which could not possibly have been investigated except for the fact that the companies were affiliated, can this Court now say as a matter of law on assumptions most unfavorable to Appellees and not agreed to by them, but which are admitted by appellant, that an earning of 8.07 per cent or 7.93 per cent is without the zone of reason, and such a rate of return as indicates the parties were not dealing at arms' length because of their affiliation?

We submit that on the valuation found by the Commission and the earnings as found by it the contract under consideration is reasonable, that the Commission and the court below should have so found, and that the Commission was without jurisdiction or power to direct the distributing companies to set up on their books any different price for gas purchased or to attempt to change existing rates on the ground of any claimed unreasonableness.

Commission's Finding of Value and Commission's Finding of Net Earnings.

In arriving at its conclusions, the Commission undertook to average earnings and average replacement reserve requirements over the annual periods ending December 31, 1930, June 30, 1931, and June 30, 1932. We insist that it is not proper to average earnings and replacement reserves as was done by the Commission (R. 164 and Com. Br. 186), and have at page 141 of this brief set out the reasons why the procedure used by the Commission is improper. Assuming for the purposes of this argument, but not admitting, that it is proper to average earnings and average replacement reserve requirements, it is our contention that even then the percentage of earning is not such as is unreasonable or such as indicates any advantage having been taken by reason of affiliation, or the contract is such as would not have been entered into by parties dealing at arms' length.

By averaging earnings and averaging replacement reserve requirements, the Commission arrived at average earnings of $8,559,669.40 (appellant's brief p. 194), from which it deducted average replacement reserves, $1,850,086.54, of which we also complain, and arrived at the figure of $6,709,582.86, which, if applied to the value of the property as of September 1, 1931, now admitted to be $74,181,902, shows a return of 9.045 per cent. In arriving at the net figure of $6,709,582.86, the Commission eliminated all payments made to Henry L. Doherty & Company under its contract requiring the payment of one and three-quarters per cent of its gross income for services rendered, and an item of $50,000.00 rate expense on account of amortizing over a period of years the expense of the proceeding before the Commission. These two items represent payments actually made by the company as appear-

ing on the books of the company, and it is our contention that they should not have been eliminated for the reason that the Commission has no power of regulation of the inter-state business of the Cities Service Gas Company, and any such elimination of its actual expenses in effect amounts to regulation. If these items are proper items of operating expense and are taken into consideration, the net earnings of the company available for return become $6,627,515.69, which is a return of 8.93 per cent on the admitted valuation.

It is our contention that the proceeding before the Kansas Commission was in no sense a rate case in which the Commission was proceeding under any lawful authority to regulate the rates of a company engaged in inter-state commerce where the inquiry would place upon the company the burden of proving confiscation, but was merely a proceeding, whether authorized or not, in which the Commission was undertaking to find out if the earnings of the Cities Service Gas Company were unreasonable to such an extent as to indicate the parties were not dealing at arms' length by reason of their affiliation. For the purposes of this argument, and assuming all facts to the greatest disadvantage to the Appellees, we submit that an earning of 8.93 per cent or an earning of 9.045 per cent are not such earnings as to permit the action taken by the Commission.

Application of Commission's Order, Commission's Finding of Value and Earnings as of June 30, 1932.

It was stipulated by the parties in the court below that if the city-gate rate of 30 cents per thousand cubic feet, as prescribed in the Commission's orders, were applied to the business of the Cities Service Gas Company

for the year ending June 30, 1932, the result would have been a decrease in earnings in the sum of $1,926,145.07 (R. 373). The net earnings of the Cities Service Gas Company for the year ending June 30, 1932, were $7,861,516.85 (R. 515). After disallowance from operating expenses of all sums paid to Henry L. Doherty & Company under the one and three-quarters per cent contract, and disallowance of the $50,000.00 rate expenses, deducting the amount agreed upon, $1,926,145.07, leaves a net income of $6,037,668.91 before replacement reserves.

The reserve allowance as found by the Commission for the year 1932 was $1,977,592, which deducted, leaves net earnings for return of $4,060,077, or a return of 5.47 per cent on the admitted value of the property. This same calculation is arrived at by Appellant in its brief, page 190. In this calculation, we have assumed that it is proper, as we contend, to determine the reasonableness of the Cities Service Gas Company contract on the experience of that company as of the date of the hearing. We have accordingly used its earnings for the last available period, the year ending June 30, 1932, and have, for the purposes of argument, accepted the Commission's unreasonably low allowance for depreciation reserves, and have assumed that the Commission was right in eliminating from the operating expenses of the company payments made to Henry L. Doherty & Company and charge made to amortize the cost of the proceeding over a period of years. On these assumptions, the earnings under the Commission's orders would constitute a return of only 5.47 per cent, which we contend is confiscatory. *United Railway & Electric Company of Baltimore* v. *West,* 280 U. S. 234.

It was the evident intention of the Commission to allow the Cities Service Gas Company earnings in excess of 7 per cent, as the Commission states in its order (R. 56)

the rates prescribed "should result in the company returning more than 7 per cent on the valuation fixed by the Commission." It was impossible for the Commission to compute such an earning on the value of the property as found by it, and in order to accomplish its purpose it resorted to the expedient of averaging values over a period of years. By this procedure, an average value of $69,724,610 was found (appellant's brief p. 194), and the average earnings were applied to this average value. We contend that it is improper and unheard-of to use average values, average earnings, and average depreciation requirements even in a rate case, and it is certainly improper and unheard-of to determine the present reasonableness of a contract on such averages. Even in normal times such procedure should not be followed, and the reasons for not doing so in abnormal times are much more readily apparent. If it is proper for the Commission to go back one or two or three years and consider earnings, there is no reason why such investigation should not antedate the depression period entirely and undertake to estimate present earnings by experience had in years of prosperity. The earnings which we have used in our argument under this heading were the actual earnings for the year ending June 30, 1932, the last available period. Since that time business conditions have failed to improve, and have steadily grown worse; operating costs under the NRA have steadily increased, and the value of the properties of the Cities Service Gas Company, as well as the properties of all the distributing companies have greatly increased, due to necessary extensions and due to higher price levels of both labor and commodities.

We submit that it is proper for this court in determining the reasonableness of the contract in question, if it is held to be an issue before this court, to do so on the

basis of the value of the property of the Cities Service Gas Company at the time the hearing was held by the Kansas Commission and the operating experience of the Cities Service Gas Company as shown by the last available figures presented at that hearing and not disputed, and if so, this court should affirm the decision of the court below on the admitted applicable facts without further examination of the record.

In the foregoing discussion we have applied the earnings of the Cities Service Gas Company to the value of its property for the purpose of showing the rate of return, and that such rate of return was reasonable. In its consideration of a reasonable rate of return, the court must bear in mind that there is a certain fundamental difference between the hazards in a natural gas utility and those in any other utility. An electric plant, for instance, can extend its facilities for the production of current at will, and can do so without making obsolete its transmission or distribution lines. A natural gas pipe line, however, must lay pipe lines, and only after they are laid can it be demonstrated whether the geological predictions as to the quantity of gas underground are, or are not, correct. Any disappearance of the gas supply in a particular field may be replaced by securing another supply from another field. But the disappearance from the first field makes valueless the transmission lines from that field. In other words, the natural gas business has a mining hazard attached to it, and to all of the money invested therein, that is not present in any other utility service. This emphasizes the time and expenditures that naturally are made by geological and supervisory forces in the choice of gas leases. The court below well expressed this idea when it said in its opinion,

> "Upon this five and a half million investment (in leases) depends the entire value of $75,000,000.00 in pipe lines, and many more millions in the properties of affiliated distributing companies."

The mining hazard above referred to is not only the hazard of the fields to which existing lines are connected becoming exhausted, but is also the hazard of closer fields being discovered which would make valueless the millions invested in reaching distant fields. As we have hereinbefore stated, the principal markets of the Cities Service Gas Company are the cities of Kansas City, Missouri, and Kansas City, Kansas. These cities are now supplied by a pipe line extending many hundreds of miles to the Amarillo gas field. Should a field similar to that at Amarillo be discovered in the immediate vicinity of this market, as has repeatedly occurred in the past, the many millions of dollars invested in the line to Texas will have to be forgotten.

Additions Which Should Be Made on Account of Failure to Apply Overheads to Lease Values.

A serious oversight was made by all engineers, attorneys, the Commission and the court below on account of the failure of all concerned to apply certain agreed overhead percentages to lease values. This oversight doubtless arose by reason of the fact that leases were computed separately and not included in valuations except by the addition of a lump sum.

It was agreed by the parties in the court below that 5 per cent was a proper percentage to be used in computing an allowance for engineering and superintendence during construction (R. 308, 375, 376, 377), and that 2.25 per cent was a proper percentage to be used in computing pre-

liminary and organization expense, administration and legal expense, and miscellaneous construction expenditures. (R. 308, 375, 376, 377.) The total of the overheads above enumerated is 7.25 per cent; and we now contend that this percentage should be computed on the proper value of the leases of the Cities Service Gas Company and added to the valuations found by the Commission and by the court below in order to correctly ascertain the values intended to be found by said Commission and said court respectively.

In addition to the application of the above percentages to the value of leases and the addition of the resulting figure to the respective values, a similar allowance should be made for the item of interest during construction. This application, however, is not that of an agreed percentage, as Hamilton, in valuing the property for the appellees used 8 per cent and Black, as engineer for the appellant, used 6 per cent as a proper allowance. Under subsequent heading, we have discussed in detail the question as to whether 8 per cent or 6 per cent should be used but in either event it is apparent that whatever per cent is determined to be proper should be applied to lease values and added to the valuation.

These overheads were computed by the Commission and by the court below on right of way for the full two-year period, it being apparent that the right of way would have to be purchased before the lines could be built. It is even more apparent that no right of way could be purchased until after leases were acquired sufficient for the requirements of the system, as otherwise, the location of the lines could not be established. If this property were to be reconstructed at this time with no property whatever in existence, the first thing to be done would be to acquire an adequate gas supply. Right of way would then be purchased to this supply and the lines laid. There is

therefore no reason whatever for not applying these overheads to gas leases. The Commission found the value of leases to be $2,874,390.00 (R. 311). Assuming for the purpose of argument that this value is correct as representing the value of the leases, there should be added to the Commission's valuation on account thereof 5 per cent as representing engineering and superintendence during construction, and 2.25 per cent representing the three items of preliminary and organization expense, administration and legal expense, and miscellaneous construction expenditures. And assuming that the Commission's adoption of 6 per cent for interest during construction is correct, there should be added an additional 12 per cent representing 6 per cent interest for the two-year construction period. These items on the Commission's own theory of their proper computation amount to $553,320.00, which increases the Commission's value of $74,181,902,00 to $74,735,222.00, and the court's value of $82,380,583.00 to $82,933,903.00.

Under the preceding heading, "Jurisdiction on the Admitted Facts," we have applied the net earnings of the Cities Service Gas Company for the year ending June 30, 1932, as found by the Commission to a value of $74,181,902,00, showing that the Cities Service Gas Company on the basis of its most recent experience was earning 8.07 per cent on the Commission's valuation, and further that if certain items were included in its operating expenses which were disallowed by the Commission, its rate of return was 7.93 per cent. Having shown that the value of the property of the Cities Service Gas Company which the Commisison intended to find was $74,735,222.00, the percentage of 8.07 per cent becomes 8.01 and the percentage of 7.93 per cent becomes 7.87, which changes make the reasonableness of the pres-

ent charges of the Cities Service Gas Company even more clear and apparent.

Under the foregoing sub-heading, "Commission's Finding of Value and Commission's Finding of Net Earnings," we have shown that using average earnings and average replacement reserves as found by the Commission and applying the resulting net earnings to a valuation of $74,181,902.00, the rate of return would be 9.045 per cent. If no eliminations had been made from operating expenses, it would have been 8.93 per cent. With the rate base increased to $74,735,222.00, these respective percentages become 8.98 and 8.87. And we again most earnestly insist that neither of such percentages constitutes an unreasonable rate of return or indicates that the present contract is unreasonable or was entered into by parties not dealing at arms' length by reason of their affiliation.

Under the preceding sub-heading, "Application of Commission's Order, Commisison's Finding of Value and Earnings as of June 30, 1932," we have shown that the application of the rates set out in the Commission's orders to the business of the Cities Service Gas Company for the last available period would produce a return of only 5.47 per cent. If the rate base is corrected for the reasons and in the manner above set out, this rate of return becomes 5.43 and is even more clearly confiscatory.

Findings of the Court Below.

As required by Rule 70½ of the Rules of Practice for the Courts of Equity of the United States, the court below made complete findings of fact and conclusions of law which were duly filed in the case. No exceptions were filed by any of the parties to these findings or

any of them, nor were any additional findings suggested by any party, and no hearing was ever requested or held for the purpose of calling to the attention of the court below any inaccuracies in the findings or conclusions as filed by the court.

When the final decree was prepared, the parties saved exceptions to certain findings as are stated in the decree, and the decree recites that such exceptions were allowed, and this notwithstanding the fact that Rule 71 of the above rules provides that nothing shall be contained in the decree other than the decree or order itself.

We call the court's attention to what was actually done in this respect so that the court may determine whether any of the parties have properly brought up for review any matters other than the findings and conclusions made and filed by the court below.

The Valuation.

Beginning with pages 31-36 of the brief for appellant several pages are devoted to an attempt to appreciate the testimony of E. B. Black, and to depreciate the testimony of F. C. Hamilton, these witnesses being respectively the engineers for the Commission and for the appellees. It is inferred that the valuation made by Black was much more complete than that made by Hamilton, and that it should therefore be given greater weight.

We had not intended to make any comments as to the relative value of the work done by these two engineers; but under the circumstances, feel required to make an answer to the statements made by counsel for the appellant.

In the first place, it is admitted that the work done by Black consisted largely of pricing out an inventory of

the property of the Cities Service Gas Company made by Hamilton and his corps of engineers and in checking maps and records furnished by them. It seems to us rather far fetched for counsel for appellant to contend that engineers who went over the whole system of the Cities Service Gas Company, inventoried every foot of pipe and every gate, valve and fitting in it, together with every building and its contents, and who prepared and furnished to Black maps showing the system as it actually existed, together with the number of miles, size and weight of the pipe and other appliances, should have made a less detailed study than the man who merely took the inventory, maps and records prepared by another and priced them out and checked them for accuracy. The work done in preparing the inventory alone required more time, study and work than was done by Mr. Black and his entire corps of engineers, and of necessity required a much more detailed knowledge of the system than anyone could possibly obtain from merely examining such inventory or such other maps and records. As to the buildings, it is stated that detailed plans were furnished by the company and were checked by Black. If Hamilton's engineers made a sufficient study of these buildings to make plans to be used by Black in his estimates, certainly it cannot be said that their knowledge and information was less than that possessed by Black who merely checked what they had done.

It seems strange to us that in order to appreciate the findings of Black and depreciate those of Hamilton, counsel for the appellant should take three or four items on which there is no contention before this court, and therefore no abstracting of evidence, and in several of which there was no contention before the trial court. One of these items was account No. 1310 where the de-

preciated value found by Hamilton was $37,194.00, while Black's figure was $35,909.00, the difference being only $1,285.00. In order to save time and expense, appellees in the court below waived this difference with the statement, "The difference between the amount claimed by Hamilton and the amount claimed by the Commission is not sufficient to warrant discussion." The court, of course, adopted the Commission's valuation on our waiver.

Another reference is to account No. 1311 where Hamilton's valuation was $50,162.00 and Black's $47,876.00, a difference of $2,086.00. Here again the Commission's figure was adopted by the lower court, as in our brief below, we state, "The difference between the amount claimed and the amount allowed is not sufficient to warrant discussion."

Attention is called to account No. 1315 where Hamilton's depreciated valuation was $385,746.00 and Black's depreciated valuation $265,746.00, the difference being $120,000.00. The court adopted the Commission's valuation, and we are not appealing from its finding.

There is nothing in the findings of the respective engineers to which counsel for appellant call attention which can in any fair manner be used as the basis of an argument that Black was more competent or more painstaking than Hamilton.

Another contention made is that the Commission had an opportunity to observe the respective engineers on the stand, and therefore were in a better position to judge the weight to be given to their testimony than was the court below. We contend that this argument is also unfair. In the court below a transcript of the testimony taken before the Commission was offered in bulk to the court without reading the same or producing the witnesses for examination. This was to save time and ex-

pense. It was not contemplated that oral testimony would have more weight or that counsel would contend as they now do. Had such contention been anticipated, appellees would have produced the witnesses and gone through all of the testimony before the court, notwithstanding the great expense and inconvenience to all parties.

If an argument that Black was more competent or careful or better informed can be based on the three or four uncontested items to which counsel for appellant have called attention, certainly an argument to the contrary can be based upon the findings made by the Commission itself in its opinion of July 20, 1932, wherein Black's figures for well equipment are increased by many thousands of dollars, due to the fact he equipped his wells with line pipe instead of casing and tubing, as is the recognized practice; that he applied the same price to plain end pipe and threaded and coupled pipe; that he entirely overlooked spare parts in compressor stations which the Commission was compelled to add to his valuation; and that he repeatedly filed amended exhibits to correct errors in previous exhibits to which his attention had been called.

It is needless to say that we do not approve of this method of attack and with these comments will dismiss the subject.

In their preliminary remarks, counsel for appellant stress the point that the findings of the Commission carried with them a presumption of reasonableness and correctness. As to this rule, we have no controversy but we insist that the court below did, in every instance where the evidence was not overwhelmingly to the contrary, indulge such presumption and adopt the findings of the Commission. This is repeatedly stated by the court

below in its findings which shows that the court gave to the Commission the full benefit of the claimed presumption.

We appreciate that the law places a presumption of reasonableness and correctness on the findings of a commission such as the one which made the orders complained of herein, but we also feel that the weight to be given such presumption depends on the circumstances of the case. The orders in question were issued by a commission composed of three members, the chairman, Mr. Greenleaf, having served on that commission and its predecessors through varying political administrations for a period of eight years, and as such commissioner had heard and determined many similar rate controversies. It is significant to note that Chairman Greenleaf refused to sign these orders and filed a dissenting opinion (R. 59). Neither Commissioner Hill nor Campbell is now on the Commission (R. 362).

On page 35 of the brief of counsel for appellant the statement is made: "In no case did the companies' witnesses give any breakdown of unit costs used by them in determining the value of this property," etc. This statement was, of course, made in a further attempt to depreciate Hamilton's testimony. The statement is not only unsupported by the record brought to this court, but is untrue. The same contention was made in counsel's brief before the Commission; and in answer thereto, appellees introduced before the Commission the full breakdown of all unit costs asked for, the same consisting of several thousand typewritten pages. A great deal of work and a great deal of expense were involved in preparing these exhibits to meet this objection; and after they were introduced, they were never opened or looked at.

So far as this appeal is concerned, the inquiry involves only four main questions, viz.:

1. The present value of the property of the Cities Service Gas Company used and useful in its business as of September 1, 1931, which the company contends amounted to $105,857,402.00; which the Commission found to be $73,170,510.00, and which the court held to be $82,380,583.00, in which figure the court included leases at cost of $5,727,272.00 instead of at their present value which the court found to be $12,000,000.00.

2. The net operating income of the Cities Service Gas Company before depreciation, which was found by the court to be $8,401,680.00.

3. A proper allowance for all depreciation and reserve requirements which the court found in the aggregate sum of $1,966,180.00.

4. The reasonable rate of return to which the Cities Service Gas Company is entitled, which the court found to be approximately 8 per cent.

The main controversy arises as to the first question, the value of the property of the Cities Service Gas Company. As stated by counsel for appellant in their brief, page 31, "All the engineers based their present value on reproduction cost less depreciation."

For valuation purposes, the property, other than cost of financing, was classified into forty accounts and items, which are listed in the opinion of the court below (303) and also on page 37 of appellant's brief. Twenty-nine of the accounts are given separate numbers, and eleven are given titles. The whole matter is greatly simplified by the process of elimination.

Of the forty accounts, there were nine accounts upon which Hamilton and Black placed identical values, which values were adopted by the Commission. These accounts

with the values placed thereon by Hamilton, Black, the Commission and the court are as follows:

	Hamilton	Black	Commission	Court
1316	$ 27,908	$ 27,908	$ 27,908	$ 27,908
1376	3,655	3,655	3,655	3,655
1380	106,035	106,035	106,035	106,035
1381	1,805	1,805	1,805	1,805
1382	23,084	23,084	23,084	23,084
1383	568	568	568	568
1385	8,202	8,202	8,202	8,202
1387	44,979	44,979	44,979	44,979
1388	21,832	21,832	21,832	21,832

Of the thirty one remaining accounts which entered into the consideration of the court below, there were nine with respect to which the difference in value between Hamilton and Black was so small that the adoption of one figure or the other could have brought about no possible difference in the final result; and for the purpose of saving time, trouble and expense, the appellees herein waived any controversy as to such items in the court below, and on such waiver the court, as a matter of course, adopted the value found by the Commission. These accounts appear below:

	Hamilton	Black	Commission	Court
1310	$ 37,194	$ 35,909	$ 35,909	$ 35,909
1311	50,162	47,876	47,876	47,876
1317	1,461	1,206	1,333	1,333
1329	155,018	133,310	133,310	133,310
1330	118,604	113,341	113,341	113,341
1334	6,835	5,633	5,633	5,633
1379	99,388	94,687	94,687	94,687
Gas in Storage	(1)	0	22,000	22,000
Working Cap.	770,126	775,000	775,000	775,000

(1) Included by Hamilton in Acct. No. 1333.

Of the twenty two remaining accounts, there were four which were arrived at by applying percentages to certain values of physical property found by the respective engineers. These percentages were agreed to by the parties and adopted by the court, so that no controversy exists as to them other than the controversy as to the base to which these percentages should be applied. These accounts are as follows:

	Hamilton	Black	Commission	Court
Engineering & Superintendence 5%	$3,166,329	$2,846,153	$2,881,000	$3,321,250
Administration & Legal	(384,586	(1,144,478	(394,084	(350,350
Preliminary & Organization (2¼	(384,586	(482,754	(480,008	(500,625
Miscellaneous Const. Exp.	(769,174	(0	(698,169	(700,769

Of the remaining 18 accounts there were five where the court, indulging the presumption of correctness of the Commission's findings, adopted them, and as no appeal was taken by appellees the same are not in controversy herein. These accounts are as follows:

	Hamilton	Black	Commission	Court
1313 (considered with 1312)	$ 573,124	$484,514	$658,439	$658,439
1315	385,746	261,887	265,746	265,746
1332	1,143,231	735,619	759,625	759,625
1384	81,448	74,481	81,448	81,448
1386	486,182	410,999	415,070	415,070

The remaining thirteen accounts or items which are controverted in the court below and which are in controversy here are as follows:

	Hamilton	Black	Commission	Court
1307.	($	$ 33,990	$ 55,982	$ 64,778
1327.	3,696,804	1,174,574	1,657,530	1,915,427
Total.	3,696,804	1,208,564	1,713,512	1,980,205
1312.	1,380,025	1,210,392	1,153,157	1,294,710
1314.	4,169,763	3,126,159	3,126,159	3,523,176
1325.	149,202	149,202	145,202	147,202
1328.	2,267,443	1,567,605	1,466,102	1,515,662
1331.	8,873,812	8,482,319	8,048,910	8,463,835
1333.	43,578,602	38,842,371	39,432,331	40,232,331
Going Concern Value	8,898,532	3,820,000	2,000,000	5,000,000
Gas Leases.	12,914,189	2,874,390	2,874,390	5,727,272

We will discuss the controverted items in the order listed.

On two of the remaining accounts, namely, taxes during construction and interest during construction, the court adopted the figure used by Black and the Commission, as opposed to the figure used by Hamilton, after having added to Black's figure depreciation erroneously deducted, and the addition of which was stipulated by the parties in the court below. The controversy as to interest is as to the rate of interest to be used during the construction period. There is no controversy as to the item of taxes. These two items as valued by the engineers, the Commission and the court are as follows:

	Hamilton	Black	Commission	Court
Taxes during Construction.	$ 769,174	$ 778,044	$ 778,044	$ 875,171
Interest during Construction.	6,337,986	3,859,204	3,883,282	4,471,934

For the item of material and supplies, the court adopted the figure presented by Black plus an addition made by the Commission of $119,275.00 covering spare parts in compressor stations which it was admitted during the Commission hearing had been overlooked.

	Hamilton	Black	Commission	Court
Materials & Supplies.	$667,371	$509,400	$628,675	$628,675

From this point on we will use the headings of appellant's brief:

1307—Production—Right-of-Way.
1327—Transmission—Rights-of-Way.

The above accounts are discussed under the heading, assigned error number 7, in appellant's brief.

In regard to these accounts, the court below made a finding of fact as follows:

> "1307-1327. (Mr. Black was the engineer for the Commission; Mr. Hamilton for the plaintiffs. Both are engineers of standing.) The Commission allowed $1.40 a rod for right-of-way. It used $1.08 as a basis, that figure being the average cost, as shown by the books of the company, of 31 per cent of its rights-of-way. To this the Commission added 22c per rod for expense of acquisition, and 10c a rod for abstracts and recording fees. The evidence clearly developed that the figure of $1.08 did not purport to represent all of the costs, and is not a dependable figure. The most dependable evidence is that of the man who negotiated for these rights-of-way during the past four years. His offering price, to all landowners, was 50c per rod for the land and 50c per rod for damages; sometimes he paid as much as $2.00 per rod for the land alone; the average damage paid was 65c. He did not state the average cost for the land, but it cannot be assumed that he acquired all of it at his offering price. It should not be figured lower than 65c, the average he paid for damages for which his offer was likewise 50c. These items make $1.30 per rod paid the landowner; adding to that the 32c allowed by the Commission for overhead, gives the figure of $1.62 which we have used. The company's figure of around $3.00 includes aerial surveys which were not used, and if used,

probably would have been worth their cost in a saving not reflected in its present valuation. Apparently, the company also included certain construction costs elsewhere accounted for." (R. 304.)

We are at a loss to understand appellant's discussion of these items as set out in its brief. The only evidence before this court is that included in the record at pages 395 to 405. This ten pages of the record is a condensed statement in accordance with the rules of this court prepared by the parties in which they have set out all evidence which they considered necessary for this court to consider in determining this issue. It is our understanding of the practice in this court that the parties are limited to the record so prepared by them in the presentation of their arguments. If so, practically all of appellant's argument must be eliminated, for there is no record whatever before this court to support the statements made or the arguments based thereon.

In the original presentation to the Commission, the evidence consisted of a valuation made by Black in which he included right-of-way at an average total cost of $0.997 per rod (R. 397). Eastman, one of Hamilton's engineers, testified that he had divided the system into nine groups in which groups a unit price ranging from $2.11 per rod to $3.54 per rod was applied to the actual number of rods in the groups respectively. Using these two methods, the value of the accounts as found by Black was $2,488,240 less than the value found by Hamilton, a difference which could not possibly exist if both engineers were properly informed (R. 395).

The experience of the two engineers making these widely divergent estimates of value and the source of

their information is stated as follows in the record at page 396:

> "As to the unit cost per rod to be applied to the number of rods in the system Black testified that he had never purchased any right-of-way and that the figures used by him were the result of information procured by his organization from other pipe line companies operating similar lines (fol. 470).
>
> Eastman, testifying as to Hamilton's valuation, testified that the figures used by him were the result of studies of the actual experience of the Cities Service Gas Company in the purchase of right-of-way in the territory under consideration, by studies of the experience of the Continental Construction Corporation in connection with its recently built line from the Amarillo field to Chicago, but he furnished no data as to the experience of any of these companies."

In an apparent attempt to reconcile this great difference in values, the Commission employed C. H. Montgomery, a certified public accountant and at one time a member of the Commission, to audit the books of the company in order to ascertain if possible the actual cost of right-of-way to it. The result of this audit was an exhibit in which the cost of right-of-way in an examination of 31 per cent of the total rods included in the two accounts was $1.08 (R. 397).

Testifying as to this exhibit of Montgomery's, Eastman stated that an analysis of job orders such as that made by Montgomery would not disclose all of the costs, as it was not the practice of the company to include in such job orders the cost of obtaining right-of-way carried on by the land and lease department, and the cost of settling damage claims and of abstracting and recording which is done by the legal department. He further

testified that the cost of securing right-of-way included all expense of men in the field, automobiles, phone calls and similar costs, and that such costs were a major item in connection with procuring right-of-way. This testimony is set out in full at pages 401 to 404 of the record.

On the testimony above outlined, the Commission was forced to the conclusion that Black was wrong in placing an average value of 99c per rod on right-of-way, and increased that value to $1.40 per rod (R. 107). In making this addition to Black's figure, the Commission not only admitted that he was in error but also admitted that the exhibit of Montgomery showing the cost of $1.08 per rod was incorrect and did not include all costs.

In addition to the testimony of Hamilton and that of Black and Montgomery, there was introduced before the Commission and the court the testimony of J. S. Gibson, who had been associated with the Prairie Pipe Line Company and the Prairie Oil & Gas Company for 22 or 23 years, and during that time had procured all of the right-of-way for said companies in a total exceeding 10,000 miles. Gibson's companies were never at any time associated or in any manner affiliated with any of the parties to this litigation, and his testimony was not in any manner impeached. Gibson testified that he had examined the cost analyses of right-of-way prepared by Hamilton and Eastman, and that, in his opinion, they were correct and reflected his actual experience except as to two items which it was not his practice to classify as entering into right-of-way costs, such items being clearing and grading, and aerial survey. The testimony of Gibson appears at page 398 of the record.

There was also introduced before the Commission and the court below the testimony of B. H. Hicks, at that time employed by the Cities Service Gas Company, his

duties being purchasing pipe line right-of-way and settling damage claims in which work he had been engaged for four years. Hicks testified that it was his practice under instructions from the company to start out to buy right-of-way for 50c a rod and 50c per rod for damages in advance; that settlement could not always be made on this basis, and that it was possible in some instances as much as $2.00 per rod for right-of-way and damages lumped together would have to be paid; and that the average damages per rod amounted to about 65c; that the average cost of acquiring right-of-way as distinguished from the purchase price was 22c, which would have to be added to the payment for right-of-way and the payment for damages. The witness further testified that he had nothing to do with such matters after the right-of-way contract was mailed to the home office, and had no acquaintance with subsequent costs (R. 399-400).

With the testimony of Black and the testimony of Montgomery discredited on account of inaccuracy, which the Commission itself admitted, and with the testimony of Hamilton and Eastman supported by their shown experience and their careful and detailed analysis of actual cost to the company, corroborated by the testimony of Gibson and Hicks who were not estimating but applying first hand knowledge acquired over years of personal experience, there can be no question but what any presumption of reasonableness which might attach to the finding of the Commission was overcome, and that the finding of the court below is sustained by an overwhelming preponderance of the evidence.

The statements made by counsel for appellant to the effect that the cost of field survey in staking the rou of the line was improperly included; that miscellaneous expenses were improperly included; that the cost of

clearing, grading and fencing was improperly included, and that other items were included improperly in the estimates by Hamilton and Eastman, are none of them supported by the record, and, of course, cannot be answered by us by reference to the record. All we can do is emphatically deny the correctness of any such statements, and ask that they be eliminated from consideration as not supported by the record, which appellant prepared.

Many like statements appear in the comments of counsel concerning which we can only make the comment that they are not supported by any evidence in the record.

It is the contention of appellees that the study made by Hamilton and Eastman of the actual experience of the Cities Service Gas Company, not of job orders alone, but of all expenses in the land and lease department, the legal department, and all other departments having to do with procuring right-of-way is entitled to the greatest weight of any testimony introduced. Their testimony did not consist of their opinion as experts as to what right-of-way costs should be, or of estimates based on hearsay information, as was the case with Black, but upon actual investigation and analysis of the experience of the company as shown by the records of its several departments. We feel that this evidence, corroborated as it was by Gibson and Hicks, should have been given greater weight by the court below and that the value of these two accounts should have been materially increased. However, the decree below was in favor of appellees, and they did not and could not appeal. We therefore stand on the finding of the court, insisting that it is supported by the overwhelming evidence.

1312—Production—Gas Well Construction.
1313—Production—Gas Well Equipment.

These accounts are discussed by appellant under the heading, assigned error Number 8.

As stated in appellant's brief, the court below added to the Commission's valuation an item of $57,233.00 on account of storage wells and an item of $84,318.00 on account of well construction generally.

In its consideration of these accounts, the Commission treated its expert, Mr. Black, rather roughly, and registered very little confidence in his judgment, considering the labored attempt previously made in its brief to appreciate his standing as a witness and depreciate the standing of Hamilton. The Commission found that Black had equipped his wells in a manner entirely unknown to the industry, and added $173,925.00 to his valuation of these accounts (quite a sizable item for an engineer at all experienced in the gas business, or as careful and painstaking as counsel have stated, to overlook). The Commission also refused to follow Black's judgment as to the item of $57,233.00 which Black had included in his valuation as the depreciated value of storage wells, and eliminated that item entirely.

The entire record before this court so far as storage wells is concerned consists of two paragraphs at page 378 of the record and a stipulation of two paragraphs appearing on page 373.

There is nothing in the record above cited upon which the argument of counsel could be based, and the only conclusion that can be drawn from the record is, that under some sort of arrangement, the details of which are not disclosed, the company has possession of and operates storage wells for which it pays the owners of the land upon which the wells are located a rental. Counsel's brief re-

fers to the contract introduced in evidence in the court below, as does the stipulation, but the contract itself is not included in the record, and this court cannot construe its terms, being unadvised as to what they are.

It is sufficient to say that the company is in possession of these wells and is using them for storage purposes under such circumstances as caused both the engineer for the Commission and the company to include them in their respective valuations and compelled the court below to reverse the Commission and put the admitted value of the wells back in the valuation. Whatever the arrangement is, it is one agreeable to both the company and the landowners, and such an arrangement as causes the landowners to recognize the right of the company to the possession of the land and its use for storage purposes. There is nothing whatever in this record to lead this court to believe that these wells so far as the hole in the ground is concerned belong to the landowners, and there was no such evidence in the court below as is evidenced by its finding.

Counsel for appellant make the further statement not supported by the record that, "If the wells cost the company nothing at the time the storage contracts were acquired, it is not reasonable to assume that the holes would have to be purchased if the pipe line system were reproduced." There is nothing in the record to indicate that the wells cost the company nothing at the time they were acquired, and the only assumption that can be made with regard to reproducing the pipe line system is that nothing of the sort being in existence, the company would have to acquire land for storage purposes and drill the required wells to put the gas in storage. It is apparent that the expense of so doing would be infinitely greater than the value now placed on these storage wells.

As to the item of $84,318.00 which the court added to the Commission's valuation, the entire record discloses and the court below found that the actual cost of well construction to the company was much greater than the amount allowed by either Hamilton or Black. After having added $173,925.00 to Black's valuation on account of Black's prices for casing and tubing being insufficient and thereby admitting that Black was in error as to the material in the account, the Commission accepted the value testified to by Hamtilton which it "corrected" by applying the overheads used by Black. This is rather a strange procedure, for if Black was entirely in error as to the prices of materials and labor in the wells, there was no reason for the Commission to believe that he was correct and Hamilton was wrong as to the overheads.

The situation as presented to the court below was this: After correcting Black's valuation by adding $173,925.00 and after returning to Black's valuation the item of $57,233.00 which the Commission had deducted on account of storage wells, the difference between Hamilton and Black was $84,318.00.

Notwithstanding the fact that Black's valuation of this account had been entirely discredited on account of the grossly insufficient amount allowed for well equipment, the appellees below introduced evidence as to the actual cost of construction of the wells which the two engineers had valued as such actual costs appeared of record on the books of the company. In addition to this showing, there was also introduced in evidence a showing as to the cost of similar wells in the same field drilled by other producers. The evidence as to the construction cost of these wells was in no sense the estimate of anyone, but consisted of actual book figures showing to a cent the amount of money which the wells in question had actually cost the

parties drilling the same. This evidence appears in the record beginning at page 379.

The Commission attempted to meet this convincing testimony by putting on the witness, Richie, a man who had never seen the wells in question, who estimated that he could drill such wells at less than the actual cost to this or other similarly situated companies. (R. 384).

The court below, therefore, had before it the valuation of Hamilton which was less than the actual cost of the wells to the company, the testimony of Black which was discredited as above set out, and the testimony of Richie who was merely estimating, just as Black did, without regard to actual experience. The evidence showed that the value testified to by Hamilton and Eastman was arrived at by analyzing the actual cost to the Cities Service Gas Company of drilling wells in the several fields and by dividing such actual costs into the number of feet drilled in order to arrive at a unit cost per foot, which unit cost was then adjusted for material and labor to present prices, and then applied to the several wells (R. 384). On this record the court could not have arrived at any conclusion other than that the valuation of Hamilton was the most accurate evidence before the court and that even his value was insufficient. By adopting Hamilton's value and putting the item of $84,318.00 back into the valuation the court was certainly acting upon evidence amply sufficient to overcome any presumption of correctness of the value found by the Commission and in accordance with the overwhelming weight of all the evidence.

1314—Field Line Equipment.

This account is discussed by appellant under its assignment of error Number 9.

The court below made a finding as follows:

> "1314. We have added $397,017 to this account. The Commission adopted Mr. Black's estimate, which was based on assumption that field lines were buried, on the average, to one-half the depth of main lines. The company's valuation was based upon the facts. Black testified his figures would have been more accurate if he had had time to gather the facts. It clearly appears, also, that field lines are more expensive to construct than main lines; they are in smaller units; more hand-labor is involved, and more connections are necessary; also the cost of field lines cannot be decreased by taking advantage of topography, as may generally be done with main lines. The *company's figures* are strongly buttressed by an analysis of actual cost of field lines utilizing 20,600 tons of pipe. The assumptions of the Commission and its engineers cannot stand against the facts." (R. 305.)

Counsel devote a number of pages of their brief in a laborious effort to show that the addition of $397,017.00 to the account by the court was erroneous. In making this argument, counsel entirely overlook the record before this court, the entire record consisting of two and a half printed pages, 388 to 390. Nowhere in this record is there any statement as to the number of feet of field lines, their size or location, or the number of yards of excavation used by Hamilton or by Black in their respective values. The entire argument is outside the record, and it is impossible for us to answer it and confine ourselves to the record. However, for counsel's information, we desire to state that all of their argument is erroneous even if the entire record before the court below is considered.

Black testified that in the Texas field he applied one half the depth of the main line to gathering (field) lines four inches and under in size and as to field lines in other states used half the depth of main lines up to 10¾ inches. (R. 389.)

Counsel state on page 59 of their brief:

> "In pricing this account, Black testified that all field lines in Texas up to and including four-inch were *priced* (italics ours) on the assumption they were buried one-half the depth of the main line."

This is exactly what Black did but is the opposite of what counsel argue. As we read the brief counsel contend that notwithstanding Black assumed field lines to be buried one-half the depth of main lines, he arrived at a greater number of yards of excavation than did Hamilton, even if his assumption was wrong, and that therefore the Company was benefited and not prejudiced and the court below should have made a deduction from the valuation rather than an addition. The error counsel make is in assuming Black estimated the yardage in field lines at one-half the yardage of main lines. He did nothing of the sort but on the contrary figured the yardage of excavation and back-fill the same for all lines and then *priced* the field line yardage at one-half the *price* used by him for main lines. In making this estimate Black concluded there were 22,902 cubic yards more than Hamilton and Eastman found by actual inspection of the lines themselves. But in valuing the main lines he used a unit cost of $0.35 per cubic yard for earth excavation and backfill, and in valuing field lines a unit cost of $0.175, one-half, just as he is quoted by counsel as having testified. This procedure resulted in a value equivalent to that which

would result from computing the total number of yards as though the trenches were one-half the depth of main line trenches, but that is entirely different from stating that Black's calculation was to the advantage of the company for the practical result is that Black used 141,486 cubic yards less than was priced by Hamilton instead of 22,902 cubic yards more as stated by counsel. Because of this, all of counsel's comparison of the yardage used by Hamilton or by the court with that used by Black is erroneous. In other words, Hamilton and Black found approximately the same number of yards of excavation to be necessary in connection with field lines, Hamilton applying thereto the proper unit cost, and Black applying thereto the unit cost he felt to be proper divided by two. This being true, the whole argument of counsel falls, whether supported by the record or not.

There can be no real controversy at this time as to field lines costing more than main lines instead of one-half as much so far as the items of excavation and back-filling are concerned. Counsel's entire argument in effect admits this but seeks to avoid the true consequences. Any doubt is removed by the testimony of A. D. Bechtel (R. 391), E. McDonald Biddison (R. 393), T. R. Jones (R. 393), and Ross M. Stuntz (R. 394). All of these witness testified that field lines were more expensive in their construction than main lines of the same size and also that any estimate as to the value of such lines based on the assumption that they were buried to one-half the depth of main lines was erroneous.

In its finding quoted above, the court said:

> "The companies' figures are strongly buttressed by analysis of cost of field lines utilizing 20,600 tons of pipe. The assumption of the Commission and its engineers cannot stand against the facts." (R. 305.)

It is our contention that under this finding the court should have added to this account $1,043,604.00 which was the difference between the value found by Black and adopted by the Commission and the value found by Hamilton after an actual analysis of company costs. As no appeal was taken by the appellees, they are, of course, bound by the court's finding; but certainly the evidence before the court not only overcame any presumption of correctness as to the Commission's finding, but warranted an addition to the valuation of a much greater sum than was added by the court.

1325—Transmission Land.
1328—Compressor Station Structures.
1331—Compressor Station Equipment.

This account is considered under appellant's assignment of error Number 10.

As to account 1325, the valutions of Hamilton and Black were identical, $149,202.00, but the Commission deducted $4,000.00 on account of its holding that the Hogshooter and Owasso stations were not used and useful. As to account 1328, Black's valuation was $699,839.00 below that of Hamilton. The valuation of Black was adopted by the Commission after they had still further reduced that valuation by the deduction of $101,503.00, Black's figure for the compressor station structures at Hogshooter, Hominy and Owasso eliminated as not used or useful. As to account 1331, Black's figure was $391,393 below that of Hamilton. The Commission adopted Black's figure after reducing it by $433,509.00 for the equipment at Hogshooter, Hominy and Owasso, which resulted in the Commission's value being $824,902.00 less than that found by Hamilton.

In the court below appellant agreed that the value of land, structures and equipment at Owasso might be eliminated, but contended that the land, station and equipment at Hogshooter was used and useful and also the land and buildings at Owasso.

The court found on the evidence that the Hogshooter station was used and useful and a component part of the pipe line system of the Cities Service Gas Company as it now exists, and put back into the valuation $2,000.00 for the land upon which that station is located (account 1325), $49,560.00, Black's value of the compressor station structure at Hogshooter (account 1328), and $414,925.00, Black's value of the compressor station equipment at Hogshooter (account 1331).

In the court below the appellees contended that Hamilton's value for compressor station structures, which was greatly in excess of that of Black, should be adopted by the court, because it was corroborated by the evidence showing the actual cost of such structures to the company and by estimates made by independent contractors. The court, however, indulged the presumption of the correctness of the Commission's finding, notwithstanding this evidence, and as to the three accounts made no additions other than to restore at Black's valuation the land, compressor station structure, and equipment taken out of Black's valuation by the Commission. As the appellees did not appeal, the sole controversy now is as to whether or not the Hogshooter station should be included as used and useful. The only evidence upon which the Commission took out of Black's valuation the land, structure, and equipment at Hogshooter is the following, as shown by the record at page 406:

> "Black introduced in evidence, as Exhibit 53, photostatic copies of sworn tax returns of the Cities

Service Gas Company to the Oklahoma Tax Commission in which reports it was stated that at the date of said returns, February 1, 1931, the Hominy compressor station was being reclaimed and that the Hogshooter compressor station 'is now and has been abandoned for several years. This property is now subject to sale and reclaim and has only a junk or salvage value of not to exceed $5,000.00.'"

It will be noted that the tax return referred to was made as of the date of February 1, 1931, and that neither by other tax returns nor by any other circumstances did anyone attempt to show that the condition which existed on February 1, 1931, continued to the time of the hearing before the court below. It is also persuasive that Black did not consider this tax return as of any evidential value or that he had outside information to the contrary, for he did include all of these items in his valuation, his inventory, of course, being made at a later date than February, 1931.

As against this evidence, if it be evidence at all, is the testimony of Eastman, set out on pages 406, 407 and 408 of the record. Eastman is an engineer who has been intimately associated with the operations of the Cities Service Gas Company for many years, and who was thoroughly familiar with its past and future plans of operation.

In the court below it was stipulated that the affidavit of George H. Baird, general superintendent of the operations of the whole system of the Cities Service Gas Company, should be treated as his testimony, such affidavit appearing in the record at pages 499 to 504, inclusive.

In his testimony Eastman went over in detail the reasons for originally building the Hogshooter station, and the reasons why it was temporarily considered as no

longer useful at its then location, and the subsequent changes in the source of supply of the Cities Service Gas Company which again made the operation of said station necessary or made necessary an increase in the capacity of other stations. This testimony is convincing, and we respectfully ask the court to read it in full as set out in the record. The substance of Eastman's testimony is set out in the following questions and answers:

> "Q. In your opinion, Mr. Eastman, is that Hogshooter station at this time useful to the pipe line project of the Cities Service Gas Company? A. Yes, sir, it is.
>
> Q. And it is the bona fide intention of the company to place it in operation? A. That is correct. I am not positive that it is in operation today." (R. 407.)

The last answer of Eastman undoubtedly is incorrectly reported, as what he intended to say was, that he was not positive that the station was not in operation today, as is shown by other testimony not quoted.

George Baird, the man in direct charge of the operations of the Cities Service Gas Company and most familiar with its then and future plans of operation, in his affidavit recites in great detail the changed situation which makes this station a necessity to the operations of the Cities Service Gas Company, a part of said testimony being as follows:

> "That on account of said extensions into Missouri and the said consequent enlargements plaintiff has been, and is holding the Hogshooter compressor station in constant readiness to serve its said pipeline systems and especially its said extensions into Missouri. That by use of said compressor station it would add a transmission capacity of approximately 20,000,000 cubic feet of natural gas daily and by such

use it can accomplish such result much cheaper than in any other manner. That while said order of the said Texas Railroad Commission is operative it will be necessary for plaintiff in cold weather to use said Hogshooter compressor station to increase the transmission capacity of its lines from whatsoever source it gets its added gas supplies, and whether said Texas order remains in force or not upon resumption of normal financial conditions or the natural growth of the Missouri markets along the said newly constructed extensions the economical operation of plaintiff's system will require the operation of the Hogshooter compressor station." (R. 503.)

With all of this direct and positive evidence to the effect that the Hogshooter station is used and useful the court was clearly right in its holding that the mere showing of a tax statement filed by the tax department of the company, entirely disassociated from the operating end of the business, was not of sufficient weight, if it had any evidentiary value whatever, to uphold the finding of the Commission that this station was no longer used and useful.

1333—Transmission—Line Equipment.

This account is discussed under appellant's assignment of error number 11.

The cost of reproduction new for this account found by Hamilton and Black, respectively (R. 415), is $46,893,014.00 and $43,099,711.00; Hamilton's figure exceeding Black's by $3,793,303.00. The present values for this same item (R. 415) are Hamilton, $43,578,602.00, and Black, $38,842,371.00, a difference of $4,736,231.00. The Commission valued the property under this account depreciated at $39,432,351.00, being an increase of $589,-

960.00 over the value found by Black, but still $4,146,271.00 less than the amount claimed by Hamilton. The addition of $589,960.00 made by the Commission was due to Black's having omitted items of painting on pipe, and to Black's not having used a sufficiently great differential between the cost of plain end and threaded and coupled pipe.

The court below, indulging the presumption that the finding of the Commission was correct, adopted the percentage condition of 90.1 per cent used by Black, as opposed to 92.93 per cent used by Hamilton, thereby disposing of $1,219,722.00 of the above mentioned difference in addition to the $589,960.00 corrected by the Commission. The remaining difference between the present value found by Hamilton and found by Black can be altogether accounted for by the difference in rock excavation, for which item there was included in Hamilton's valuation $4,211,120.00 (R. 307), and in the Black valuation $1,270,115.00, Black being lower than Hamilton by $2,941,005.00. This difference is accounted for partially by the greater quantity of rock excavation found by Hamilton, and partially because of the higher price applied to the yardage of rock excavation which Hamilton used. The court resolved the difference so far as price was concerned in favor of the Commission, thus again indulging the presumption that the Commission's finding was correct, although the court expressed itself as not entirely satisfied with the figure used (R. 307).

The finding of the court as to this account is as follows:

> "1333. The difference between the engineers' valuations of this item is about $4,000,000. The dispute narrows down to three items: (1) The Commission

found the property to be in 90.1 per cent condition. The company asserts it to be in 92.93 per cent condition. The Commission's finding is supported by the testimony of its engineer, and a consulting engineer called by the company. We approve the Commission's finding as to per cent condition. (2) The cost of rock excavation. There was a dispute among the experts, but the Commission's finding is supported by the testimony of its engineer and a contractor who had done much of this work. Elaborate comparisons of costs of selected lines are introduced to show the error in the Commission's cost figure. But the results depend largely on the lines selected. While not entirely satisfied with the figure used, we are not disposed to disapprove the finding as to the cubic yard cost. (3) There is a difference between the engineers as to the amount of rock excavation in the lines. After the hearings before the Commission, engineers for both sides drilled a hole every quarter of a mile along a main 125 miles long. That extensive investigation developed that the percentage of rock excavation was 20.94 per cent instead of 10.46 per cent used by Black. If overcuts are included, the percentage is 28. We are inclined to believe that overcuts should be excluded; it is probable that contracts for trenches would be predicated on the trench depth, and would not call for overcuts caused by the inability to blast to a neat line. This additional evidence convinces us that Black's estimate of the amount of rock excavation is too low. His estimate on the line used for the test was 24,000 yards; Hamilton's was 72,482 yards. The test showed on Black's own figures, exclusive of overcuts, 46,790 yards. The subject is not capable of exact proof, but we are of the opinion that Black's amounts of excavation should be materially increased. Mr. Hamilton's valuation of rock excavation is $4,211,120; Mr. Black's $1,270,115, of which $1,154,503 is in this account. Applying

> Black's price to an increased amount indicated by the test, results in an increase of this item from $39,432,331 to $40,232,331." (R. 307.)

There being no appeal by appellees, the present controversy is limited to the third item in the above finding—the amount of rock excavation.

There was no evidence before the Commission other than that testified to by Black, Hamilton and Eastman. Black's qualifications as set out on page 419 of the record are as follows:

> "Black testified with respect to classified excavation that he determined the percentage of such excavation by observation of the territory through which the major part of the line passed and from his knowledge of the territory (fol. 494) gained through more than twenty years of experience. He testified that he made a personal inspection of line 'G' from Wichita to Ottawa; that he allowed $2.50 per cubic yard for all classified excavation whether solid or loose rock and had allowed this amount in addition to ordinary cost of trenching and backfilling of ditches of the same dimensions."

The estimates of Eastman and Hamilton were made in the manner and from the sources of information set out in the record at pages 416 and 417, in part as follows:

> "Eastman testified that the amount of rock excavation shown by Hamilton's valuation was determined by engineers sent out over all the lines for that purpose and who procured their information from surface observations and from talking with company employees who had been in charge of maintenance work for years and from repeated excavation of the lines were familiar with soil conditions. That where shoot-rock was shown in the valuation

it had been calculated as solid from top to bottom of the trench, and that where pick-rock was shown the entire excavation had been calculated as pick-rock. That he developed a unit of cost of $7.38 per cubic yard for shoot-rock and $4.01 per cubic yard for pick-rock. Mr. Eastman further testified: * * *

"'We did not attempt to determine rock excavation on a percentage basis. At the beginning of this work, we sent four engineering parties into the field for the purpose of checking lines. These parties were each composed of two graduate engineers, and they went over these lines in detail, in many cases walking the length of the line, together with the district superintendent of that district, or his foreman, or the line walkers. They went over each line and every line in detail to determine the amount of rock excavation on that particular line.'"

It would appear from the foregoing qualifications of the respective engineers and the nature of the investigations made by them respectively that the valuation of Hamilton should be given much greater weight than that of Black. Throughout the entire case before the Commission there had been no instance in which its attention had been called to mistakes made by Hamilton or his engineers in the valuation presented by them other than the contention that prices used were too high. On the contrary, it had been shown to and was admitted by the Commission that Black was mistaken as to his well equipment, on account of which many thousands of dollars were added to his valuation; was mistaken as to the differential to be applied between plain end and threaded and coupled pipe, which resulted in a difference of $589,000.00, corrected by the Commission itself; was mistaken as to the cost of right-of-way, on account of which mistakes the Commission corrected his valuation

in the sum of $494,948; and was mistaken, as is in effect admitted by counsel in their brief, in assuming that field lines were buried to one-half the depth of main lines.

In connection with his study of observed depreciation in order to ascertain the percentage condition of the underground part of the pipe line system, Hamilton had his corps of engineers spend many weeks in going over the system uncovering the pipe and taking samples or coupons therefrom in order to demonstrate the actual depreciation the pipe had sustained. In doing this work 1328 excavations were made to the pipe, such excavations being distributed throughout the entire system. In addition to this, detailed studies were made of reports covering 16,330 excavations made in the course of ordinary maintenance work through a period of recent years. These studies were all made in connection with the determination of depreciation; but as that issue was eliminated by agreement in the court below, the evidence was not brought to this court, counsel for appellees not having anticipated the attack which would be made on the account under discussion. These studies in connection with depreciation gave Hamilton and his corps of engineers information in regard to the rock in the system which could not possibly have been attained by Black and his engineers.

Notwithstanding this showing as to the relative competency of the two engineers, the Commission eliminated from Hamilton's valuation $2,941,005.00.

There being such a great and inexcusable difference in the amount of rock excavation found in the two valuations and the Commission having cut so deep, the appellees decided to find out what the actual facts were. Black had testified as above quoted that he had personally

inspected line "G," 125 miles of line from Ottawa to Wichita, and taking his word for it that he knew more about this line than any other, appellees decided to have an actual impartial test made of it. A truck was equipped with a compressed air drill and an independent and disinterested contractor, George P. Reintjes of Kansas City, Missouri, was employed to assemble the necessary help and proceed to ascertain the truth. Black and Hamilton were invited to attend or send a representative so that all parties would be equally advised and no advantage could be claimed to have been taken by anyone. Both Black and Hamilton sent engineers, and the test proceeded. This party, with representatives of both engineers, sank 291 holes (R. 431), observed the actual conditions existing and Reintjes made his reports as appears in the record at page 431. This report showed conclusively that Black's allowance of 10.46 per cent should have been 20.94 per cent (R. 433) and that if the necessary over cuts were included in the consideration, the percentage should have been 28 per cent, the percentage of over cuts as shown being 7.09 per cent.

We had hoped that this actual test would settle the controversy, but it only brought forth another flood of argument such as is contained in appellant's brief. It had to be admitted, of course, that Black's allowance for this particular line, which the Commission adopted, would have to be more than doubled, but the contention was resorted to that this test had no probative value as to the balance of the system, and this, notwithstanding the fact that the line was selected which Black said he personally inspected.

The court below was greatly impressed by the results of this test, as is shown by the finding quoted above, and after considering this evidence in connection with the

record before the Commission, restored $800,000.00 to the valuation, leaving $2,141,005.00 which it did not allow.

The court allowed nothing for over-cuts, although that item alone would amount to an addition of $560,000.00 to the valuation. The court did not find that such over-cuts were not proper, but merely stated, "We are inclined to believe that over-cuts should be excluded; it is probable that contracts for trenches would be predicated on the trench depth, and would not call for over-cuts caused by the inability to blast to a neat line." (R. 307.)

This reasoning of the court assumes that these lines would be contracted, and not built by the company itself, which is an assumption that Black refused to recognize throughout his valuation, as he at no time allowed any amount for contractor's profit.

In addition to the doubt expressed by the court as to over-cuts the court was not satisfied that $2.50 was a proper allowance for rock excavation, but adopted that figure by reason of its indulgence again in the presumption that the finding of the Commission was reasonable. The language of the court is: "While not entirely satisfied with the figure used, we are not disposed to disapprove the finding as to the cubic yard cost."

By reason of having eliminated over-cuts and having adopted the price of $2.50 per cubic yard for rock excavation, the court eliminated from the valuation many thousands of dollars. The appellees, therefore, feel that the allowance made by the court for this account is entirely inadequate, but as no appeal was, or could have been, taken, the finding of the court below must prevail. Nevertheless, all of these considerations should be given their due weight in determining whether or not the result finally arrived at is unduly favorable to appellees.

The entire argument of the appellant with respect to this account is, that the results of the actual test made on line "G" cannot be applied to the system as a whole without leading to an apparent absurdity. That the actual facts when the system as a whole is considered could not be determined without a similar test on every mile of line in the system is apparent. It is also apparent that applying the demonstrated results of this test to some particular line chosen by appellants for the purpose results in apparent absurdity. However, none of this argument in any way lessens the value of this test as to the correctness of Black's conclusions as applied to the line which he said he personally inspected, and which line was chosen for the test by reason of the fact that it was the only line he did personally inspect. Neither is there anything in the record or in counsel's argument to indicate that this test applied to the system as a whole would not result in an approximately correct conclusion, which conclusion would add a comparable amount to the rock excavation in Black's valuation. The test not only demonstrated the amount of rock in the ground, but the percentage of error in the engineer, which percentage can be fairly applied to his finding of rock excavation in the whole system.

There is no question but that in the system as a whole there are many sections in which rock predominates, and other sections in which there is substantially no rock. Either party could, for the purpose of argument, select some section of the system and apply to it the proven percentage of rock in some other section, and demonstrate conclusively that such percentage was not applicable. However, it is reasonable to assume that taking the system as a whole, the percentage of rock is substantially the same. There is no record before this

court containing evidence that the system as a whole should not properly be judged by the 125 miles in line "G," although that section of line was not selected as a representative section, but was selected because Black had personally inspected it and had more knowledge with respect to it than any other line. However, it is a representative section as to that part of the system in which rock is known to exist, and for the purpose of demonstrating, as it did demonstrate conclusively, that Black's allowance should be more than doubled in order to reflect actual value.

Appellant's discussion is confined almost entirely to an attempt to show discrepancies by applying the test on line "G" to other parts of the system. Counsel completely overlook the fact that appellees introduced evidence as to the actual cost to the company of eleven major lines constructed in recent years (R. 426). The purpose of this showing was to demonstrate, and we believe it did conclusively demonstrate, that the actual labor costs to the company in the construction of these lines were materially greater than were the labor costs allowed by Black, and that Black's failure to approximate these actual costs resulted largely from his failure to properly estimate rock excavation.

Black's affidavit (R. 440) admits that his rock excavation for line "G" was low by $56,972.00, which is 11.86 per cent of the out-of-pocket cost of labor on this line, as testified by T. R. Jones (R. 420). Appellant's discussion of these costs attempts to show that the addition for rock excavation made by the court below resulted in an absurdity when applied to certain specific lines. Those lines which were listed in the record (R. 426), wherein a comparison was made between labor costs shown by Hamilton, the actual expenditures made

by the company in the construction of the lines, and labor costs shown by Black, do not permit any such conclusion. Below are listed seven lines on which the actual labor costs were analyzed, and which lines were comparable to line "G" in that they ran through adjacent territory and through territory that did necessitate rock excavation.

This tabulation shows that the inclusion in Hamilton's valuation for labor on these lines was $1,408,772.00, and that the actual expenditures for labor by the company for the same lines was $1,398,638.00, a difference of $10,000.00, or less than .8 of 1 per cent.

Black's inclusion for labor in his appraisal of these lines was $1,057,173.00; and his figure thereby varies from the actual cost by $341,465.00. To his figure there should be added 32.3 per cent to bring his estimated labor costs up to what the actual costs of construction were.

This tabulation, instead of proving that the court below erred in allowing too much for rock excavation, shows that its addition of $800,000.00 to Black's valuation was very much below the amount which should have been added. The tabulation to which we have referred above is as follows:

Name of Line	Comparison of Labor Costs Hamilton	Actual Cost	Black	Per Cent Increase of Actual Cost Over Black
Ft. Scott 8"	$ 194,736	$ 215,959	$ 139,639	54.66
Springfield 10"	489,809	427,633	343,085	24.64
St. Joseph 12"	190,224	170,286	157,268	8.28
St. Joseph 16"	58,582	67,080	43,803	53.14
So. Trunk 16"	111,172	111,098	86,459	28.50
Topeka 16"	192,177	206,107	144,869	42.27
Ottawa-Lawrence Jct 20"	177,072	200,475	142,050	41.13
Total	$1,408,772	$1,398,638	$1,057,173	32.30

The figures found by Hamilton compare favorably with the actual cost to the company of the eleven lines ana-

lyzed, corroborate his findings and discredit the findings of Black. This is also true as to the results of the test on line "G" if overcuts are included, as set out in Reintjes's report, in which event the findings of Hamilton are not, as stated by counsel, as much too high as the findings of Black are too low.

When estimates and opinions refuse to be reconciled, there is but one recourse and that is to the facts, if available. The facts in this case have been shown by the test of line "G" and actual labor costs in the construction of the lines which the engineers estimated. These facts must be much more persuasive than estimates.

Engineering and Superintendence During Construction.

This account is discussed by appellants under assigned error No. 12. The finding of the court below appears in the record, page 308, as follows:

> "Engineering and Superintendence is stipulated by the parties to be 5 per cent of the value of the properties excepting accounts Nos. 1316, 1380, 1381, 1382, 1383, 1384, 1385, 1387 and 1388. The parties have stipulated that this and other overheads should not be depreciated. Accordingly we have computed overheads by applying the Commission's percentage to the undepreciated values of the property, using $66,425,000."

There was no controversy as to this account except as to the base to which the agreed percentage should be applied. The court applied this percentage to $66,425,000.00, whereas appellants contend it should apply to a much greater value to be determined by this court's consideration of the matters herein set out.

To be corrected as shown in this brief, page 48.

Preliminary and Organization Expense.

The finding of the court was as follows (R. 308):

> "Preliminary and Organization Expense. We adopt the Commission's finding of ¾ per cent of the values of the physical properties; and for Administration and Legal Expense, ½ per cent on physical values, including engineering; for Miscellaneous Construction Expenditures, 1 per cent, on same values."

The percentages recited in the above finding have been agreed upon by the parties. No controversy exists as to them other than the controversy as to the base to which the agreed percentages should be applied. If the value found by the court below is sustained by this court, the lower court's allowance for this item should be adopted, although in the court below it was our contention that the base should be substantially greater. If this court should find that the court below should have included leases in the rate base at their present value instead of their cost or should make other additions, such agreed percentages should be applied to the addition so made.

To be corrected as shown in this brief, page 48.

Administration and Legal Expense During Construction.

This account was included by the court in the finding quoted under the preceding heading and what we have stated with respect to the previous account applies hereto.

To be corrected as above stated.

Miscellaneous Construction Expenditures.

Same as stated under preceding heading, with same correction.

Taxes During Construction.

No controversy.

Interest During Construction.

The finding of the court with respect to this account is as follows (R. 308):

> "Interest during construction. The Commission used a rate of 6 per cent, the company 8 per cent. It is customary to calculate this item at the prevailing rate charged a person with good credit for temporary advances, which is now 6 per cent. This throws upon the borrower, the owner of the property, the hazard of the borrowed money during the construction period, which must be considered. Two per cent is a reasonable allowance for that hazard, but it is customary and preferable to make this allowance as a part of Going Concern Value. The parties have agreed that this item, as well as taxes, should not be depreciated. We have taken the Commission's figure, increased by 6 per cent on the difference in values found, approximately $200,000."

The record with respect to this item consists of the evidence abstracted on pages 442 and 443 of the record and the evidence with respect to a proper rate of return appearing in the record at pages 528 and 529.

In his valuation of this item, Black used 6 per cent as a proper charge for interest during construction, and Hamilton used 8 per cent. Both engineers used approxi-

mately a two-year construction period, Black applying 6 per cent and Hamilton applying 8 per cent to the average investment throughout the two-year period, which was equivalent to applying, respectively, 6 and 8 per cent to all the property for one year. The court below found that 8 per cent was a necessary rate of return for the company (R. 317) after the plant was placed in operation and in effect found that 8 per cent was a proper charge for interest during construction, the court dividing the charge into 6 per cent as the cost of money and 2 per cent for the hazard of carrying the investment. The court states in its finding, "It is customary and preferable to make this allowance (2 per cent for hazard) as a part of going concern value." We do not believe the court is correct in finding that it is customary or preferable to so handle this account and believe the court should have valued this account by applying 8 per cent to the value found by it. It is, of course, immaterial to appellees whether this allowance is included in interest during construction or in going value, but in its consideration of going concern value as hereinafter discussed the court must bear in mind that included in the allowance made by the court below is an allowance of 2 per cent for interest during construction and in considering the allowance for going concern value the court should deduct therefrom $1,490,545.00, which is one-third of the 6 per cent allowed by the court under interest during construction, to-wit: $4,471,934.00.

Interest during construction is that portion of the return to which an investor is entitled which is capitalized during the period prior to the time when the property goes into operation. During the construction period when there are no operating revenues, the investor has

no method by which he can secure a return on his investment in any other manner. During this period he is denied any return on his investment and, therefore, the courts and Commissions have approved the allowance in the rate base of an amount equal to that return of which he is deprived as a part of the cost of the project to the owner.

The return on the money which the investor sacrifices during the construction period is just as much a cost to him as is the money which he furnishes for the construction of the property. The rate at which he should be compensated for that sacrifice logically must be the rate that is considered a fair return on the property after it goes into operation.

As a practical matter the cost of money borrowed for construction purposes always exceeds the cost of money borrowed on the same type of property that is in operation with customers attached and a history of successful operation behind it.

Allowances for interest during construction at low rates have been made at times by Commissions who were confused because of the fact that an operating company with a large amount of property and a successful operating record behind it sometimes borrows money to construct an additional plant and is able to secure it at prices as low as, or lower than, what has been determined to be a fair return. The confusion arises from the fact that the reason such loans are made is not based on the security back of the loan which will be furnished by the property to be constructed, but on the security and credit which has been established by the other and larger amounts of property which have been constructed in the past and which already have a successful operating record.

No bank would loan money at any rate of interest to a company which could pledge as security only the property to be constructed for that money, because ultimately it would have as security for its loan an amount of property equal only to the original loan itself with no margin whatever to secure the interest to be paid on that money. The loans that are made by banks are secured either with collateral far in excess of the loan or are made to a company whose credit has been established by its ownership of property far in excess of the loan. The interest rates of such loans are no indication of the fair return to which an investor is entitled for the sacrifice of return on his money during the construction period in a project, the success of which can only be demonstrated after the construction period is ended and after a period of successful operation.

The risk which the investor who furnishes construction money takes is the risk that the property may never become a successful operating unit.

The only distinction between interest during construction and rate of return is the fact that interest during construction is that portion of rate of return that arises during the period when there is no revenue out of which the investor may get any return and for that reason it is capitalized as a part of the cost of the project.

There are no prevailing rates for a loan of this nature for no such loans are ever made. The chance the investor is taking is greater before the construction is completed than after at least a temporarily successful operating period has passed. Chance has more to do with rates in a case of this nature than the security of the property to be constructed, for the greater part of such cost is labor, and if the project is not successful the security behind the loan is not what the property cost but its

junk value. All labor cost is lost and added to that loss is the labor necessary to salvage the material.

But, even should it be argued that current rates should be used, what is the current rate for such a project? The project of the Cities Service Gas Company is long past the stage of promotion and speculation. The Commission says its earnings are excessive. The Commission's engineer says the property is in such condition, both as to lines, gas and market, that it cannot be criticized. Yet the bonds of this established project are now selling for a price that will bring in a return of 11%. If such is the criterion by which interest during construction should be judged, certainly 8% is reasonable and 6% is entirely unreasonable.

We submit that Hamilton's use of 8%, being corroborated by all other witnesses in the case, including the Commission's witness, Montgomery, this court must find that the necessary capital to construct this project could not be attracted at less than 8%, and that 8% is the proper rate to use for this item.

This item is subject to correction for overheads as hereinbefore stated at page 48 of this brief.

Going Concern Value.

The evidence before the Commission consisted of the testimony of Hamilton who valued this item at $8,898,532 (R. 443) and the testimony of Black who valued the item at $3,820,000 (R. 443). The Commission in its finding disregarded the testimony of both engineers and used an arbitrary figure of $2,000,000, which is included in the valuation found. The court below increased this allowance to $5,000,000.

It is argued in appellant's brief that a smaller allowance should be made for going value in the case of a company engaged in the production, transportation and sale of natural gas than should be allowed in the case of utilities generally. The reasoning back of this argument is that the Pipe Line company, being engaged in the business of supplying distributing companies at the city gate found the business already in existence; and that all that had to be done was to make a connection at the city gate of the distributing company. This argument is fallacious for many reasons. For the purpose of discussing this phase of the question, we propose to divide the distributing companies into four different classes, and consider them from the standpoint of common knowledge and experience.

First, distributing companies in towns which have at some time in the past used natural gas and where the customers therefore may be supposed to have some familiarity with its benefits, but who because of the loss of natural gas facilities have a considerable skepticism about again equipping their houses with natural gas burning appliances.

Secondly, those towns where natural gas was being supplied from another source at the time of the construction of the pipe line under consideration.

Third, those towns being supplied with manufactured gas service, and

Fourth, those towns which had not up to the time of the pipe line's being constructed had any gas service.

After careful consideration of these four classes it will be found that sales do not come to the pipe line like Mr. Bryan's "million men springing to arms overnight." The pipe line has no draft to replace the customer's failure to volunteer. Certain towns in which gas is being

supplied by the Cities Service Gas Company pipe line such as St. Joseph, Missouri, had had experience previously with natural gas. Their supply had failed due to the financial or engineering inability of a predecessor company to maintain a line across the Missouri River. The town had been left without heat on several occasions. Whatever investment the customer had in heating appliances was lost, and he had thereafter used artificial gas for a period of ten years or more, for cooking and either coal or oil for his heating requirements. A moment's thought will convince anyone that it would take a long time to build the load up to what should be the normal heating load in a town which had passed through such an experience. It also would be a waste of investment to build a pipe line to the town to supply only the needs indicated by the quantity of artificial gas sold and at a later date have to replace that pipe line with a larger one to take care of the volume of gas which represents a normal natural gas heating load.

Let us now consider class two, where a town has been educated to the use of natural gas supplied by another company. One of two things must necessarily follow: If this present company is to secure this business, it must be because of a willingness to make price concessions, or secure the business through very superior salesmanship or because the service from the other company has been very unsatisfactory. If the service from the other company has been very unsatisfactory, there will be the same long period to go through in the restoration of such confidence on the part of the customer as will result in his investment in the amount of natural gas heating equipment which will permit him to burn a normal amount of gas under good service conditions. Under the other two conditions, price cuts or superior salesmanship, the

acquisition of the business will require long negotiations and expenditures of much time and intelligent effort.

In the consideration of class three (an artificial gas distribution system), the attempt to supply that town with natural gas brings the owners of the distribution system immediately face to face with the proposition that the large sum which they now have invested in their artificial plant becomes not used and useful property, and we know of no one who can cite any particular case where stockholders have greeted this proposition with any applause. It will require long negotiations with the city council and the distribution system owners before even a contract can be made.

It next will require a period during which the distributing company must expend money to increase the size of its mains which have been fully adequate to supply the amount of artificial gas burned, but which are entirely inadequate to supply the quantities of natural gas that will be burned. It is naturally impossible to sell natural gas househeating appliances until such time as the pipe line is connected to the distributing system and natural gas is available and it is equally impossible to have all of the customers at once buy househeating equipment. It takes a period of several years to reach the normal saturation of house heating installations from the standpoint of a natural gas supply, when natural gas is taken to a town previously supplied with artificial gas.

In the consideration of class four, it will be recognized that if no gas at all has been served previously to the arrival at the town border of the pipe line, a company must be formed, a distribution system must be designed, financed and built, customers attached and equipment sold to those customers for the utilization of gas. In all of these cases engineering and sales talent must be

supplied to the distributing companies by the pipe line company, for one or more of several reasons; first, because there being no previous company there is no personnel familiar with the problem connected with the sale of natural gas, for even the artificial gas men's viewpoint must be directed to house heating and they must be educated as to methods and equipment necessary to get the required volume of natural gas sales.

In a town previously supplied with natural gas and where the supply had failed, there must be a large amount of sales effort on the part of the pipe line company to convince customers that this present pipe line will give adequate and continuous service before they will make their investments. This is something the pipe line must and the distributing company cannot do. To any except the very largest cities only one pipe line is built and this forces the pipe line company to spend money to facilitate the acquisition of the load as rapidly as possible because of the penalty they are under from the excess investment which they have up to the point where the load reaches the amount of gas for which the pipe line was designed, such design being based of course on the normal consumption of natural gas per customer.

The appellant has quoted in its brief the following testimony by Hamilton in an effort to contest the allowance by the court below for going concern value:

> "Q. Do you mean to say, Mr. Hamilton, that every plant of the same value should have the same allowance for going value? A. No, because there would be a very different allowance between your pipe line plant or your distribution plant or an electric plant or something like that. There might be a wholly different basis.

Q. For instance you take the distribution plant, take the one here in Topeka, for example A. Yes, sir.

Q. If you assumed that you would reproduce it now, and it had no customers, it would mean you would have to attach in that case, thousands of customers before the business was established? A. That is true, and 10 per cent allowance in that distribution plant would not be sufficient, in my judgment.

Q. Then take a pipe line company like this, and the number of customers you have is not very large, very many involved, don't exceed three or four hundred? A. That is true.

Q. That should be taken into consideration in arriving at the Going Value in this case? A. That is true."

In this testimony Hamilton said: "Different plants would have different allowances for pipe line plant, distribution plant or an electric plant * * * There might be a wholly different basis." Following that counsel by accident or otherwise chose one of the four most profitable distribution centers of the line from among 135 on which to base his question to which Hamilton replied "a 10 per cent allowance in *that* (italics ours) distributing system would not be sufficient in my judgment." A ten per cent allowance for going concern value even on the Commission's valuation would amount to $6,930,000.00, but on the above testimony the appellants are endeavoring to reduce the court's allowance which was only $5,000,000.00. The appellant then goes on to quotations from the testimony such as the following:

"Jarboe, superintendent of all pipe lines of the system, testified that the line to the Amarillo field was constructed for the purpose of taking care of the present demand of the pipe line system.

Hamilton testified:

'Q. The line from Amarillo to Wichita, that as I understand, when it was built, was built for the purpose of taking care of the demand for gas you had at that time? A. Yes, sir.'

Mr. Eastman testified as to the Amarillo line from Texas to Wichita and Ottawa:

'Q. Now this line was built to Texas; was any addition to the market procured from that line, were any additional markets procured, any new customers? Are there any connected to that line between Texas and Wichita? A. No new cities; there may be a few small towns along that line served, but they are inconsequential.'

'Q. Was there any other purpose than to supply existing markets?' A. No.'

From the above testimony, appellants argue that there is no delay in attaching business. However the addition of the following testimony (R. 451) must be connected with the above testimony as to certain specific lines to get the complete history of these lines:

"Q. The line from Amarillo to Wichita, that, as I understand, when it was built, was built for the purpose of taking care of the demand you had for gas at that time? A. Yes, sir.

Q. You already had the demand for gas, and the Amarillo line was put in for the purpose of taking care of the demand at that time, that had already accumulated? A. To take care of it, based on the disappearing supply with which we had previously been taking care of it.

Q. I understand that, but the Oklahoma line was built (fol. 525) to take care of a demand that you then had for gas? A. Yes, it was with the idea of supplying ourselves with gas at a cheaper price than we had been forced to pay, otherwise, before this field came in.

Q. You already had the demand for the gas? A. Yes, and we already had a source of supply, but this was a cheaper source."

The present towns are being supplied with gas from fields that were not in existence until many years after the beginning of natural gas service to these towns. Fields have come in, pipe lines have been run to them, the fields have declined, then disappeared, new fields have been connected and the pipe lines to the old fields have been taken up. It is a constant program of change in the case of a company as large as the one under consideration. The fact that these particular lines have been built to replace a supply which previously had been taken from other fields and which was rapidly declining or that they had been built to replace an expensive gas supply with a supply at a lower cost, has no bearing whatever on either the cost of attaching the business to the pipe line or on the value above the physical property value which a willing buyer would pay a willing seller for that business so attached.

If a pipe line has been in existence for years with business attached and a history of profitable operation behind it, that pipe line has an admitted going concern value. If then that pipe line is replaced with another by reason of the failure of the field to which the first was connected, what then becomes of this admitted going concern value? It can truly be said of the second line, as appellant argues, that it was built to an existing market. But that is an entirely different matter from saying that the second has no going concern value. It has, in fact, all the old line had and more too, because it now has a real gas supply behind it.

Instead of the percentage allowance for going concern value being less in the case of the Cities Service Gas

Company than in the case of a usual utility as contended for by appellant, we insist that the reverse is true. The ordinary utility servicing the inhabitants of a city is a self-contained unit. It either manufacturers or purchases the commodity which it distributes and sells and its operations are more simple, its operating force being merely that required to keep its machinery and plant in proper condition.

On the contrary, the plant of the Cities Service Gas Company and its organization is most complex and its problems such as to require the greatest foresight on the part of its operating officials and the greatest coordination between the different units making up the system as a whole. In the first place, available markets had to be studied and analyzed to determine whether they were such as would make the project economically feasible. After that was determined, it was necessary to acquire an adequate supply of gas to supply the system because in the absence of such supply the system would have no value whatever.

Not only would such supply have to be procured originally, but throughout all the years the company has been in operation it had to be maintained and guaranteed not only for the present but for the future. In addition to all this, the various sources of supply attached to the system had to be so coordinated that all cities served should at all times have an adequate supply of gas. The plant of the Cities Service Gas Company is not a single unit but consists of one unit whose duty it is to procure and maintain a supply of gas, another unit whose duty it is to maintain the system in proper operating condition, another unit whose duty it is to dispatch the gas through the system and regulate pressures and supply to all cities without regard to their location, and another

unit whose duty it is to see that sufficient gas is sold to produce earnings for the requirements of the company.

The Cities Service Gas Company now has and for years has had an organization which functions efficiently as to all of these various operations. This organization keeps in touch with the present and future requirements of all cities attached to the transportation system and plans with them for their present and future needs. Without this organization, failure of service would result just as it did result some years ago before the different pipe line companies now composing the transportation system came under the present ownership and were coordinated, and before there was an over all organization looking at the problems of production and consumption from the viewpoint of both the producer and the consumer. If the plant of the Cities Service Gas Company were to be reproduced as of September 1, 1931, none of this organization would be in existence. There are few men trained in the natural gas business and capable of becoming members of the present organization, and it would require years of time and an infinite number of costly errors before an organization such as the present one could be assembled and before the resulting service to consumers would reach the state of perfection now admitted.

The investors in the old Kansas Natural Gas Company lost many more millions of dollars than we claim for going concern value because they did not have such an organization.

What, then is the value of this organization, and what should be allowed for going value in this respect. What also is the value to the company of having markets attached which are developed to such an extent that the use of gas has doubled or trebled its use in the artificial

gas days. Without either the organization or the market, the whole project would be a failure.

We are not attempting to place a specific value on these items for obviously that can not be done. We do state however, that the argument of counsel that the going concern value which should be allowed in this case is less than the allowance that should ordinarily be made to a public utility, consisting of one self-contained unit, is ridiculous.

In addition to the remarks we have made as to the value of the present organization from an operating and service standpoint, we also desire to emphasize the great saving in operating expenses which has resulted from the consolidation of the former separate units into the present system. Prior to the time the present owner acquired the property now under consideration, the system consisted of several unrelated and separately operated units the principal of which were the Kansas Natural Gas Company, the Wichita Natural Gas Company, the Wichita Pipe Line Company, the Marnet Mining Company, the Quapaw Gas Company, the Kansas City Pipe Line Company and the American Pipe Line Company. Each one of these companies had its separate officers and operating organizations instead of the one organization now operating all of them.

The Commission allowed $2,000,000.00 as the entire going concern value to which the company is entitled. We have no hesitancy in saying that the operating expenses of these combined companies including salaries to executives have, by reason of their consolidation, been reduced more than $200,000.00 per year. A saving of $200,000.00 per year in operating expenses if capitalized would be equivalent to $2,500,000.00 going concern value at a rate of 8 per cent.

During 1928, 1929 and 1930, several large natural gas projects were built. It is a matter of common knowledge and court record that several of these projects are now in the hands of receivers, although the lines were designed by the best engineering firms in the United States, were connected to a plentiful supply of gas, and ran to cities with large populations.

The principal reason of their failure was an inability to connect customers at a time when coal and oil, the two competing heating fuels, were selling at the lowest price within recent history, and therefore natural gas had no price advantage to offer from the standpoint of operating cost to the householder, and, secondly, the resistance on the part of the householder to the necessary expenditures for gas heating appliances during a period of great depression.

Those lines have the same type of pipe and compressor stations as the company under consideration and have an adequate supply of gas, but are failures because of the lack of connected load. Therein lies the difference represented by Going Concern Value. It is the difference between physical property ready to operate and not operating and the same physical property with a normal load connected and operating. This difference is insurance that the tremendous expenditures for gas acreage, pipe lines, compressor stations, et cetera, can be made to earn a return and we believe that it is an obvious fallacy to argue that a factor that gives that insurance to eighty or more millions of dollars of property should have a value as low as $2,000,000.00.

Assuming that the other lines referred to above should weather the depression and should at a later date succeed in connecting the load for which they were designed, the loss of return for one year on an $80,000,000.00 property,

due to the failure to have a connected load, would alone amount to $6,400,000.00. The depression has already lasted *four* years and may last longer so that the company under consideration has had a return of $25,000,000.00 above what it would have had if the item of going concern value had not been present in the property at the beginning of the depression.

During this period of depression, prices of labor and material are obviously low and a determination of the value of physical property as of that time naturally results in a valuation being found lower than that which would be reached if the determination was made during a period of prosperity; however, going concern value differs from this and particularly so in regard to a utility rendering natural gas service, the utilization of which is predicated on large expenditures on the part of the customer.

This is obvious because if a pipe line company were to attempt to attach customers during a period of depression it would meet an additional sales resistance caused by the disinclination of the public generally to spend money for new and different household equipment. Customers attached with houses equipped for the utilization of natural gas furnish a going concern value higher in a period of depression than in periods of prosperity due to the increase in the difficulty and therefore the cost of creating that going concern value during such a period.

The brief for the appellant gives considerable space to the question of interest during construction for which the court allowed 6 per cent and the difference between that amount and the 8 per cent which was found by the court below to be a return within the zone of reason. It is contended that 6 per cent for interest during con-

struction is ample because of the ability of a person or persons with credit to borrow money for construction purposes at that rate. Having by their argument contended for 6 per cent as the amount to be allowed for interest during construction they object because the court below included an additional 2 per cent under going concern value, to recompense that person or persons for the risk which they took in putting their credit back of the project.

They make no suggestion as we see it as to the proper place for the inclusion of this item for risk and their brief necessarily leads to the conclusion that that person or persons who supply this necessary credit are to go without any compensation at all. This would predicate the construction of future pipe lines on the willingness of philanthropists to devote their funds to the realm of speculative investment.

The appellant further devotes a considerable portion of its brief to a discussion of the court's inclusion of an item to cover the depreciation of that portion of the plant which is idle during the process of attaching business. In our estimation, this is directing their discussion to the cost of attaching business which may or may not have any relation to the value of the business after it is attached. The question before the court is the question of the value of the business attached and we have directed our discussion to that value.

Hamilton, who testified to a value for this item of $8,898,000, was, as is shown by his testimony as to his qualifications, occupying a position where for years he had had charge of purchase and sale of a large number of properties and his determination of the going concern value of the Cities Service Gas Company property was

based upon his experience and represented his judgment of the value which a willing buyer would pay and a willing seller accept over and above the value of the physical property of the system. That judgment was not affected by his knowledge that predecessor companies had spent many millions more than his allowance in endeavoring to create this going concern value.

In the foregoing discussion, we have undertaken to list merely a few of the elements entering into going concern value as applied to the property of the Cities Service Gas Company which are not common to utilities generally. We will now discuss briefly the usual allowance made by courts and commissions for this item.

In the recent case of *Denver Union Stockyards Company* v. *U. S.*, 57 F. (2d) 735, the three-judge court which had the matter of going concern value under consideration in its opinion gives a tabulation citing six recent decisions of this court, the value of the properties involved, the amount allowed for going concern value, and the percentage such allowance for going concern value bears to the value of the property. This table is as follows:

	Cost of Reproduction	Amount Allowed for Going Concern Value	Per Cent of Going Concern Value to Cost Reproduction
Knoxville v. *Water Co.*, 212 U. S. 1, 29 S. Ct. 148, 53 L. Ed. 371.	$ 538,000	$ 60,000	11.1
Omaha v. *Omaha Water Co.*, 218 U. S. 180, 30 S. Ct. 615, 54 L. Ed. 991, 48 L. R. A. (N. S.) 1084.	5,700,583	562,712	9.9
Denver v. *Denver Union Water Co.*, 246 U. S. 178, 38 S. Ct. 278, 62 L. Ed. 649.	10,617,782	800,000	7.5
Georgia Railway v. *R. R. Comm.*, 262 U. S. 625, 43 S. Ct. 680, 67 L. Ed. 1144.	5,250,000	441,629	8.4
Bluefield Co. v. *Pub. Serv. Comm.*, 262 U. S. 679, 686, 43 S. Ct. 675, 67 L. Ed. 1176.	324,428	32,442	10.0
McCardle v. *Indianapolis Water Co.*, 272 U. S. 400, 47 S. Ct. 144, 71 L. Ed. 316.	14,904,000	1,366,000	9.17

This court, in the case of *McCardle* v. *Indianapolis Company*, 272 U. S. 40, said:

> "The evidence is more than sufficient to sustain 9.5 per cent for going value. And the reported cases showing amounts generally included by commissions and courts to cover intangible elements of value indicate that 10 per cent of the value of the physical elements would be low when the impressive facts reported by the commission in this case are taken into account."

It is apparent from the testimony of Black with respect to the matters taken into consideration by him in fixing the allowance for going concern value that he did

not take into consideration the matters we have above suggested showing the difference between the going value allowance which should be made the Cities Service Gas Company and the allowance usualy made to public utilities which consist of an independent self-contained unit. His valuation of this item we therefore contend is insufficient.

In making his valuation of this item, Hamilton did not attempt to place values upon the different elements to be considered as such estimates would of necessity be mere guess work. No one can say exactly what the value is to the Cities Service Gas Company of having its existing markets attached, of having its properties under one company and under one management as against many companies with independent managements, or the value of having its production and consumption requirements coordinated as they now are coordinated. He contented himself with the rules laid down by this and other courts and took for his valuation of this item 10 per cent of the value of the physical property as he found it to be. It is our contention that even this valuation is low for the reason that allowances made utilities generally are not applicable to the property of the Cities Service Gas Company.

We submit that the Kansas Commission had no right to ignore all the evidence before it and to arbitrarily fix a value of $2,000,000.00 on this item, which is an allowance of less than 3 per cent. The members of this Commission are not presumed to be experts or to know anything about the method of arriving at such valuation. If they were such experts or were supposed to exercise their own independent judgment without regard to the evidence there would be no purpose in introducing evidence at all.

In addition to the evidence introduced before the Commission, appellees employed the firm of Ford, Bacon and Davis, Inc., nationally-known engineers, to make an investigation and study of the property of the Cities Service Gas Company and its history for the purpose of determining a proper allowance for this item. Such a study was made and in the court below it was stipulated as follows:

> "It is further stipulated that the witness James A. Emery will testify that he is vice-president and director of Ford, Bacon and Davis, Inc., engineers; that he was employed by the complainants herein to make a study of the property of the Cities Service Gas Company for the purpose of determining the proper allowance for going value and that in the opinion of said witness going value should be allowed in a sum between eight and a half and nine million dollars."

The court below therefore had before it as the only evidence in the case, Hamilton's testimony to a value of $8,898,532.00, Black's testimony to a value of $3,820,000.00 and Emery's testimony to a value of between $8,500,000.00 and $9,000,000.00. On this evidence, it is our contention that appellees were entitled to an allowance for this item in an amount much exceeding the $5,000,000.00 allowed by the court.

Gas Leases.

With respect to gas leases, the court below said in its opinion:

> "The commission held that certain gas leases claimed to be held by the Cities Service Gas Company for gas reserves were in excess of the required

reserves, and that they were in fact being held for speculative purposes. The evidence established, and we have found, that the officers and directors of the Cities Service Gas Company, who are men of broad experience in the natural gas business, in the exercise of an honest and, we think, sound business judgment, determined that such leases were necessary to afford it an adequate gas reserve, and that such leases were acquired and are held by it as bona fide reserves, and not for speculation.

The commission was not empowered to substitute its judgment for that of the officers and directors of the Cities Service Gas Company as to the amount of leases necessary to afford an adequate gas reserve, in the absence of a showing of abuse of discretion by such officers in that regard. *Southwestern Bell Tel. Co.* v. *Public Service Com.*, 262 U. S. 276, 289; *State Public Utilities Com.* v. *Springfield Gas & Elec. Co.*, 291 Ill. 209, 234, 125 N. E. 891; *People* v. *Stevens*, 203 N. Y. 7, 96 N. E. 114, 117; *Idaho Power Co.* v. *Thompson*, (D. C. Ida.) 19 F. (2d) 547, 580; *Kansas City K. V. & W. Ry. Co.* v. *Bristol*, 101 Kas. 557, 167 Pac. 1138, 1140; *Denver Union Stockyard Co.* v. *United States*, (D. C. Colo.) 57 F. (2d) 735, 748."

The finding of the court as to gas leases is as follows:

"*Gas Leases.* The company owns the gas rights in about 1,202,000 acres, excluding 59,000 acres bought for the Texoma Company, in which the Cities Service Company is interested. Of these, 42,297 acres are developed; 196,170 acres are proven; 25,607 are in probable territory, and 998,287 acres are classed as of prospective value only.

Many experienced witnesses, testifying for the plaintiffs, valued these leases at figures, the average of which is $12,914,189, of which $1,996,574 represents the 998,287 prospective acreage. Mr. Holl

testified for the Commission as to values; he was a practical geologist and oil man with no personal knowledge of the fields in question, and no particular experience with gas leases. His testimony was predicated on a trip he made to the fields for the purpose of testifying, and inquiries made on that trip. He valued the leases at about one-third of the company's value. The Commission valued them at $6,279,237, of which $998,287 was for prospective acreage. The Commission valued the Amarillo holdings at $4,281,894; the Hugoton holdings at $556,116. The cost of the leases, after deducting those bought for the Texoma Company, was $5,727,272.

The Commission excluded all but 71,267 acres from the rate base. The holdings of the company at Amarillo alone are 94,820 acres. The acreage allowed is valued by the Commission at $2,874,390. The Commission arrived at this result by finding the amount of gas left in the Amarillo holdings, based upon the estimate of geologists; it deducted from the company's requirements, gas now being purchased by the company from other producers; and found that the gas in the acreage allowed would serve the customers for twenty-two years.

The Commission found that the remaining leases were acquired for speculative purposes, a finding based upon one fact: the Texoma Company was formed by the Cities Service Company and other interests to build a pipe line to eastern states; leases were acquired by the Cities Service Gas Company for its affiliate, and later transferred to it. On the other hand, in this court, is the uncontradicted sworn statement of responsible officials that all the acreage was acquired as gas reserves for this pipe line. There is also the significant circumstance that not a single lease, acquired for that purpose, has been sold. We hold, therefore, that these leases were acquired, and are held, in good faith, for this pipe line, and that the finding that

they are held for speculative purposes is contrary to all the evidence.

We further find there was error in eliminating these leases from the properties of the company because the company is now contracting some gas, and conserving its own. The first duty of the company is to see to it that its patrons have an adequate supply of gas. To insure this, it must own the gas. Contracts for gas are well enough when gas is plentiful, but when the shortage comes, contracts are not adequate safeguards. Broken contracts will support verdicts for damages, but they will not heat the houses nor cook the breakfasts of the patrons in Kansas. The company has not only the right, but is under the duty, to own enough gas to meet the needs of its customers.

Who shall determine what reserves are adequate? A commission, with no moneys invested, or the owners of this pipe line which, without gas, is worse than useless? Within the limits of reason, undoubtedly that determination must be left with the owners. Perhaps they have been over-cautious, but if error is to be made, it should be on the side of ample reserves. The owners of this property had seen the gas exhausted from field after field; they had seen their customers lost because the supply had failed; they had seen fields of great promise belie their expectations. They had seen geologists wrong before. In recent years, they had seen the state prorate the taking of gas. The Commission's figures are predicated on a 20 per cent recovery; within two weeks of its order, the Texas Railroad Commission cut this to 4 per cent. What the future may hold, by way of state action, no one knows. We cannot say the owners did not, in good faith, acquire this acreage to protect their great investment and to insure their patrons a dependable gas supply. They invested around $4,500,000 in 200,000 acres in proven or probable territory, and about a million more in a million acres in prospective territory. Upon this

five and a half million investment depends the entire value of $75,000,000 of pipe lines and many more millions in the properties of affiliated distributing companies. The Hugoton field is not now connected with the pipe line; but it is a field of great potential supply, is favorably situated, and the investment therein is not large. We find that all the acreage owned is used and useful in the public service.

The value of it is problematical, as is true of all gas properties. If the Amarillo field stands up, it is probably worth the value placed on it by witnesses for the company; if it stands up, then that field is adequate for the needs of twenty years; it may not stand up, and the company acquired Hugoton and other acreage against that eventuality; if it does not, it is not worth so much. Its value depends upon a future market, and on the actions of state commissions. The overwhelming weight of the competent evidence sustains the valuation of the company, around $12,000,000. That is about twice its cost. For the purpose of this case, and upon the authority of *United Gas Co. v. Railroad Commission*, 278 U. S. 320, we have put the gas leases in at cost. The figure is arrived at by subtracting from the cost of all the leases, the cost of those transferred to Texoma, which leaves the cost of those now held."

The findings of the court are so complete and comprehensive and the reasoning of the court in its opinion is so clearly stated, that there is little we can add. We certainly do not propose any attempt to analyze the maze of conflicting figures presented by the record or the comments of counsel thereon.

In connection with the consideration of gas leases, we again desire to call the attention of the court to the nature of this proceeding, if its nature can really be determined. The Commission admits it has no jurisdiction

over the inter state rates of the Cities Service Gas Company except in determining local rates, and admits that local rates are not now in question. The Commission admits also that it cannot regulate this company engaged in inter state commerce, and it is apparent that for that reason the Cities Service Gas Company was not made a party to the proceedings before the Commission, and was given no opportunity to introduce any testimony or make any explanation with regard to its methods of doing business.

The State, represented by the Commission, is not the owner of this property, and has no responsibility with respect to the service rendered by it. In this period of unrest and general disturbance, there is no question but what a Commission responsible only to the political officer which appointed it could secure great public acclaim and approbation if it could reduce the rates paid by the residents of Kansas for gas; and it is also quite apparent that such action on its part could be used to great political advantage. At page 226 of the record appears a statement made to the Commission by an attorney representing the distributing companies, which, if this court will read, will give a very clear understanding of the situation which existed at the time this proceeding was commenced.

The Cities Service Gas Company is engaged in no business other than the production, transportation and sale of gas. It is not engaged in the business of purchasing and reselling gas leases. As the court found, there is no evidence in the record of even one sale made by the company for speculative purposes. This being true, what possible consideration would induce the officers of the company who are responsible for service to purchase needlessly leases which they would not, in their bona fide

business judgment, consider necessary for the protection of the investment and the protection of service? The procuring and holding of the leases in question involved not only their original purchase price, but involved the continuous annual rentals necessary to be paid in order to hold them, running into many thousands of dollars annually. It is the admitted purpose of the officers of this company to make money for the owners of its stock and securities. It is a corporation organized for profit, and there is no other excuse for its existence. In the furtherance of this purpose, it must have been at all times the intention of these officers to operate the company as economically as possible in order that reasonable earnings would result. It is also evident that the owners of the stock and securities of this company would not long tolerate uneconomical operation or needless expense. All of these matters must have been in the consideration of the officers of the company when the existing leases were purchased, and must be taken into consideration by any commission or court giving the matter consideration.

As we have previously stated, the Kansas Commission has no responsibility with regard to service. The tenure of office of the members of the Commission is usually short lived and entirely dependent upon politics, as is evidenced by the fact that the only two members of the Kansas Commission who signed the orders in question herein are no longer members of that Commission. It is easy for such members having no knowledge whatever of the gas business and being more concerned with their continuance in office than in service, to say that the officers of the company abused their discretion in purchasing gas leases and were overly concerned as to their responsibility for rendering service, but clearly any action taken by such Commission, if authorized under any cir-

cumstances, should be action based on the evidence in the case.

The evidence in the record before this court consists of testimony and stipulations in which are set out the judgment of the responsible officers of the company as to the necessity for these leases. There is a stipulation as to the testimony of H. O. Caster of Henry L. Doherty & Company (R. 370), the affidavit of H. R. Straight, vice-president and general manager of the company and its highest local executive (R. 497), the affidavit of Ross M. Stuntz, superintendent of production (R. 493), and the affidavit of George H. Baird, general superintendent of operations over the whole system of the company (R. 499). All of these men are operators nationally known and recognized for their ability. They each and all say that in their judgment the existing leases of the Cities Service Gas Company were purchased after the most careful investigation and for the reason that in the opinion of all such officers their purchase was necessary in order to make service certain. The testimony of these men in connection with the fact that no consideration other than usefulness could have possibly influenced their judgment is entitled to, and must be given, great consideration. This is an unregulated company which could have no possible purpose in padding its assets for rate purposes.

As opposed to the testimony of these men, there stands alone the testimony of F. G. Holl who was employed by the Commission to give the testimony which he did give. We have set out in detail in the record (R. 473-8) the qualifications of Holl with respect to the expert testimony which he gave. From this testimony it appears, as the court below found, that Holl was a practical man who, prior to his employment by the Commission, had never

been to Texas, and who knew no more about the value of leases or the necessity for them than any non expert whom the Commission might have employed. What Holl did was, to go to Texas and talk with such persons as he chose to contact for the purpose of getting their ideas on the subject. None of these persons contacted appeared as witnesses, and we do not even know that the opinions expressed by Holl reflected anything that was told him by anyone. As we view his evidence, it is the rankest kind of hearsay, and the Commission should have excluded it on the motion of the distributing companies, as set out in the record at page 477.

The only experience to which Holl testified which would, in any sense, qualify him to testify as an expert, was, that for some years he was employed in a most subordinate capacity by this very company. If, while occupying this subordinate position, Holl had had the temerity to approach the officers of the company with the suggestion that they were purchasing more leases than were necessary to safeguard service, the result can be easily imagined; but that is exactly what this man is now undertaking to do, and his testimony is the only testimony in the record which could possibly be construed as supporting the findings of the Commission that any part of the existing reserves were not necessary. Even Holl did not testify to that effect. All that he did was to produce for the benefit of the Commission a great array of figures purporting to show the amount of gas in reserve, and the Commission, using these figures and assuming that at all times the company could take from the ground through its wells a certain percentage of the open flow thereof, found that the leases were in excess of actual requirements.

The calculations made by the Commission, however, failed entirely to take into consideration any future contingencies. No consideration is given to the fact that other pipe lines may be built to these same reserves which would rapidly deplete them. No consideration is given to the fact that the reserves may be dissipated and exhausted by the practices of oil operators. And no consideration is given to the fact that state laws may be enacted which would so limit the amount of gas which could be taken from the reserves as to entirely change the Commission's calculations, based on 20% of open flow.

That the action of state legislatures in limiting the amount of gas to be taken from wells is not mere idle conjecture, we call the court's attention to the order of the Texas Commission appearing in the record at page 496, under the terms of which the takes from wells are limited to 4 per cent of the open flow. This order, as we understand it, is still in litigation; but if it should be sustained by the courts, the great reserves of the company in that state, which the Commission has found to be ample for years to come, would immediately become inadequate. That this is true clearly appears from the affidavit of Mr. Stuntz. (R. 493.)

In addition to the matters above discussed, there is another consideration which the Commission has entirely overlooked. The Commission in its opinion, and counsel in their brief assert that it is unnecessary for the company to own all of these leases for the reason that an adequate supply could be contracted from others. This argument entirely overlooks the fact that the reason for there being gas available under purchase contracts at the prices being paid is, that the major pipe line companies, such as the Cities Service Gas Company, have their own reserves which are ample for their requirements. If it

were not for these reserves, and if the major pipe line companies were dependent upon producers not associated with them in any manner, such producers taking advantage of the pipe line companies would fix the price of gas at such a figure as would make it impossible for the present rates to local consumers to be maintained. It is only the fact that the companies have these reserves which make these prices possible.

At page 91 of appellant's brief, the statement is made:

> "This is not saying that the officers are to be criticized for purchasing these leases, nor is it contended that if the time ever comes when said gas leases are in fact devoted to the public use, they should not then be included in the rate base on which to determine a rate."

In support of this statement, several cases are cited, where property owned by a utility but not then used was excluded from the rate base. Those cases, however, were rate cases in which the Commission was exercising its right of regulation, which does not exist in the case at bar.

The thought which must immediately suggest itself to anyone reading the above statement of counsel is, if the officers of the company are not subject to criticism by reason of having purchased these leases (which is equivalent to saying that they exercised their bona fide business judgment in purchasing them), where is the money to come from for the purchase of these leases and for the payment of annual rentals necessary to hold them. The company is engaged in no business other than the sale of gas. It has no income except from that source. If the officers are not to be criticized for having purchased the leases and if it was proper for them to purchase the same,

how are they to be paid for? If the above argument of counsel for appellants is carried to its conclusion, it is equivalent to saying that the officers are subject to criticism and for that reason the leases should be abandoned.

A further thought which suggests itself in connection with this argument is, that if the leases should be included in the rate base at the time they become useful, at what figure are they then to be included? These leases, or many of them, were purchased years ago, and have been held by the company through the intervening years at great expense. The reason for this is, that when a gas field is discovered, leases must be immediately purchased if they are to be purchased at all at a reasonable figure. Should the reserves of the Cities Service Gas Company, or any other similar company, become inadequate in any year, that fact would immediately become known, and everyone owning leases would immediately become advised that the company had to have leases, regardless of the price, as without a gas supply its entire investment would be lost. If, under these circumstances, the company should enter a gas field and undertake to purchase leases on a large scale, it would have to pay prices entirely out of line with the present value claimed for the leases which it owns, and the rate base when that time arrived would by reason thereof be much greater than the rate base now claimed. The reasoning of the Commission and its attorneys is based on the assumption that these leases are only necessary for future use. The consideration is entirely overlooked that many of these leases now in use were for many years held as unproductive and for use in the future, which future has now become the present.

We submit that in a proceeding of this sort where no power of regulation exists as to a company engaged in interstate commerce, the Commission is without power or authority to substitute its judgment for that of the officers of the company in the absence of a clear showing that the judgment of such officers is not bona fide.

As to the value of the leases constituting the reserves of the Cities Service Gas Company, the evidence consisted of the testimony of 10 witnesses who were chosen because their experience made them thoroughly familiar with such values. The substance of the testimony of these witnesses is set out in the record at pages 464-468. These witnesses, with one exception, did not attempt to fix values by speculating as to the amount of gas in reserve and the possible market for same or the prices for which such gas could be sold in such market. They were men who had bought and sold leases in the various fields, and who were familiar with the present market value of such leases. We will not undertake to analyze this testimony, or to state anything further with respect to their qualifications, which are well stated in the record, to which we have referred the court.

As opposed to this testimony of disinterested men most qualified to testify, is the testimony of F. G. Holl, the man sent by the Commission to visit various fields of which he had no knowledge for the purpose of forming an opinion from conversations picked up on the street.

On this record the court below found the overwhelming weight of evidence to be that the present market value of the leases of the Cities Service Gas Company was $12,000,000.00. The court did not, however, include the leases in the rate base at this figure, but at their actual cost to the company of $5,727,272.00. This, the

court did on the authority of *United Gas Company* v. *Railroad Commission,* 278 U. S. 320. As we read this case, this court adopted cost as against present market value for the reason that the present market value was not properly established. It was with this case in mind that the appellees procured witnesses who were qualified to, and did, testify positively as to present value based on actual purchases and sales. We believe that this testimony is clearly distinguishable from that in the case relied upon by the court below, and that the court should have added to the rate base $12,000,000.00 for leases instead of the cost figure which it did add.

We desire to refer briefly to the authorities cited by appellant in support of its contentions regarding gas leases, to point out their inapplicability to this case, and to call attention to the misinterpretation of counsel as to the holding of the court in the respective cases and the reasoning behind such holding.

The first case cited is that of the *Spring Valley Water Company* v. *San Francisco,* 165 Fed. 668. This was a case in which the rates to be charged by the Water Company were the matter under consideration, the Commission having jurisdiction to determine such rates and jurisdiction to regulate the company, which is not the situation in the controversy at bar where the Commission has no such power or jurisdiction. Further, the property in this case which was claimed not to be used or useful was land bought for some future construction purpose and which since its purchase by the company had appreciated from a cost of hundreds of thousands of dollars to millions of dollars. The court said the company should be satisfied with this bargain without including the land in the rate base. It must be borne in mind that this land had no purpose other than any

other land in any other location which the company might have bought. It was not purchased because it contained water necessary for present or future use, but solely as the location of some future dams and aqueducts. This land or dam site could have been immediately sold without in anywise affecting the company's present or future ability to render service. Another location could have been purchased when its use became necessary. In the case at bar, gas reserves were purchased only for the reason that reserves were necessary to guarantee immediate service and service over the immediate future, and were purchased and accumulated into a reserve at the only time they could be acquired. The company could not dispose of these leases now and subsequently repurchase them or similar leases at anything like the values now claimed. The present situation is entirely different from that under consideration in the case cited, and the case has no application to the present controversy.

The next case cited is that of *Acquaokanonk Water Company* v. *Board of Public Utility Commissioners,* 100 N. J. L. 169, and is another case in which a water company, whose rates were properly under investigation and whose operations were subject to regulation, purchased a site for future use. All that we have said with respect to the Spring Valley Water Company case is equally applicable here.

In the case of *Chesapeake & Potomac Telephone Company of Virginia* v. *Commonwealth,* 136 S. E. 575, the telephone company purchased a corner lot in the city of Richmond upon which it contemplated erecting a building in the future. The lot had nothing whatever to do with present service or with guaranteeing future service. The company could at any time sell this lot

and purchase another or purchase any one of thousands of buildings in the city which could be made to serve its purpose. Since any one of these corner lots could be purchased at that time in the future when its use became necessary, there was no reason for burdening the operating expenses with the carrying charges up to the time when the use of the lot became necessary. If the Cities Service Gas Company were now claiming that there should be included in the rate base a lot which it had purchased with the expectation of erecting a building thereon at some time in the future, this case would be applicable; but it certainly is not applicable to gas reserves in connection with the purchase of which counsel state the officers of the company are not to be criticized, because of the fact that gas reserves are available only when and as gas is discovered.

The next case cited is the *Grangeville Electric Light & Power Company*, P. U. R. 1922 D, 513, and is merely the decision of a state commission, unworthy to be cited to this court and not now worthy of our comment. However, in this case a dam was built with a capacity in excess of the needs of the customers attached. Since the dam capacity is a continuing item, the excess capacity would never become used and useful for the present number of customers, and must have been built in the expectation of the addition of other and different customers. This is directly contrary to the reasons on which the reserve leases were acquired for the Cities Service Gas Company. Those reserves are necssary for the continued service to the present number of customers attached to the system.

The next case cited is that of Columbus Gas & Fuel Company, being a decision of the Public Utilities Commission of Ohio. The order of the Commission in this

case was reversed by the Ohio Supreme Court, and, as we understand, an appeal therefrom is now pending in this court.

The case of *City of Erie* v. *Public Service Commission*, 278 Pa. 512, 123 Atl. 471, is cited and quotations are made from the opinion by counsel for appellant. We believe this case in point on the questions here presented, although it was a case where rates were involved and the company concerned was clearly subject to regulation by the state commission. We know of no case where a court has given more careful consideration to the question as to whether cost or present value should be applied to gas reserves in determining a rate base; and if the reasoning of the court in this respect is right, as we believe it is, the court below was clearly in error in putting into the rate base gas reserves at their cost of $5,727,272.00 instead of their present value of $12,000,000.00. The court in this case also gave careful consideration to the question of leases used and useful in the public service as distinguished from leases held in reserve; and we believe counsel for appellant have entirely misconstrued the opinion of the court in this respect. As we read the Erie decision, its reasoning approves the allowance of all of the gas reserves of the Cities Service Gas Company in the rate base at their present value. Clearly, counsel is in error in stating that

> "* * * the main controversy was over gas holdings, which were included in the rate base at a valuation nearly $6,000,000.00 lower than the lowest estimate of their value shown by the testimony in the case." (Appellant's brief, 134.)

What the court says in its opinion is, that the lowest value placed on leases under the evidence was $11,212,-

000, and that the Commission allowed only $5,500,000. The difference between the evidence and what the Commissi allowed was, as counsel state, nearly $6,000,000; but this finding of value by the Commission was not approved by the court, but was expressly disapproved in the following language:

> "The Commission must in some measure be controlled by the evidence before it. An order is not in conformity to law if based on reports not offered in evidence and not the subject of cross-examination. *Pennsylvania R. T. Co.* v. *Public Service Commission,* 78 Pa. Super. Ct. 593; *Pennsylvania R. Co.* v. *Public Service Commission,* 69 Pa. Super. Ct. 404, 411. A finding without evidence is arbitrary and baseless (*Interstate Commerce Commission* v. *Louisville & N. R. Co.,* 227 U. S. 88, 91, 57 L. Ed. 431, 33 Sup. Ct. Rep. 185) and a mistaken conception of the legal effect of evidence is equally fatal."

We consider this decision so well reasoned on the issue of whether the Commission in the case at bar should have excluded any part of the reserves as not used and useful, on the issue as to whether cost or present value should be used, and on the issue as to whether the carrying charges on all leases are properly chargeable as expense items, that we desire to quote from the decision at length.

> "In ascertaining what part of the value of the gas lands not presently in service should be included in the rate base, we must consider the purpose for which the additional holdings were acquired and the physical characteristics unique to this class of lands. There may be something inherent in the land, its peculiar qualities, or the use

that differentiates this from other properties. We may assume these properties were acquired for the interest and benefit of the rate-payer, as well as the company. Gas is a fugitive substance; it has no fixed situs; when drawn from one well it may come from any part of the territory, as it flows from one well or piece of land to another. When gas escapes to other fields, the former owner's title is lost. As each year's use diminishes the supply, so one part of the tract becomes exhausted, and the entire field related thereto may be exhausted. Gas sometimes lies in a pocket in a known gas field. In this it differs from coal, ore and other minerals, and is more like oil. There is no means of reproducing the product when once taken from the earth. The company gets only the gas inclosed in the reservoir, and there is no known means of determining the quantity inclosed therein. Like many utilities, its strategic, so distinguished from its monopolistic, position in its chosen field may be an added circumstance, not only as to value, but how much should be included in present value. While productivity may be considered, its place is and should be in value, and the market or present value should, and as we read the evidence did, take in these conditions. Because of these qualities, while it may be possible to presently determine the value of the lands, in fixing the probable proportionate amount of future life of the entire tract applicable to used, useful and fair reserve, it may be, and no doubt is, impossible to delimit it with any degree of certainty, either in acreage or value. There can be no graduated values of gas lands fixed as a rate base under any theory presented to us that will consider property presently used and a descending ratio until exhaustion appears that is not the result of a pure guess. Beyond that proportion of the lands reasonably necessary to the company's life, the rate-payer should not be required to assume the remainder as a burden. Though this may

be difficult to determine, the Commission, acting as an administrative body in each case, must decide the question, as in all other matters subject to the right of appeal.

"One thing of importance must not be lost sight of. Whether the gas lands be valued or considered on a reservoir or acreage basis, the gas is not paid for as gas until it is brought to the surface and used. In addition to the fair return on the rate base as found, there is added payment for the corpus of the estate taken away, or gas that is taken out, used and cannot be replaced. This is taken care of in an allowance for 'depletion.' The fair return on the rate base is a fair return to the company for the money invested. It does not include any sum to repay capital outlay; it only pays for the use. This must follow, for a *reasonable part of the gas holdings not being presently consumed but essential to the future life of the company, the carrying charges with incidentals should be allowed in the rate.* We know of no more equitable rule for the amount to be fixed as its rate base, certainly one fraught with less difficulty, than the present value theory adopted by the courts. It applies with equal fairness to the consumer and to the company; for if these lands may be disposed of to others at present value, the owner should not be denied compensation on a similar basis. These charges are of the same character as those embodied in what is known as fair return. The consumer not paying for the product until actually removed is not paying for what some one will later pay. The purpose for which the lands are bought must be fairly essential to the life of the business.

"Suppose we adopt the theory of original cost as to these lands; it would be just as incorrect fundamentally as that of present value for the complaint is against paying any return on the value of what will be used in the future. If, as stated, original cost includes all gas lands, we meet the

difficulties mentioned in another part of this opinion, wholly unfair to the owner, as well as consumer, where that cost is exorbitant. In new fields of unknown duration, suddenly developing a large output, the highly speculative feature of these lands is well known. 'The purchase of additional gas rights,' treated 'as operating charges,' places on the present day consumer an undue burden, particularly when the prices paid are high. It enables the company to recoup immediately its capital outlay. If, in addition, we carry forward the cost as a part of the rate base, or recovery is permitted through depletion, when we allow an additional return on capital already in the pockets of the owners.

"If we give no return on any value for these lands, the owner for a given number of years receives nothing for an investment upon which the life of his and the consumers' organization depends. Not until it is used is he paid, and such payment is based, under the rule, on the then present value. This value will not include compensation disallowed during the years the property stood waiting to be used. Market value is not built on any such consideration. There is no scheme advanced whereby the owner may recover the interest, other outlays, or the return on present value." (Italics ours.)

We submit that this case instead of holding, as is indicated in appellant's brief, decided the presented issues for the appellees.

In the case of *Logan Gas Company* v. *Public Utilities Commission of Ohio*, 169 N. E. 575, the Supreme Court of Ohio did, as stated by counsel, reject certain classes of leases as not used and useful, but did so on the authority of the Ohio statute, "which requires the property to be given valuation to be both 'used and useful.'"

Counsel for appellant comment at considerable length on the decision of the court in the case of *United Fuel*

Gas Company v. *Public Service Commission of West Virginia*, 14 Fed. (2d) 299. In this case the court did, as stated by counsel, eliminate from the rate base the value of certain leases which it held to be not used and useful. However, an appeal was taken to this court which resulted in the decision reported in 278 U. S. 322. As we read the decision of the court, it did not approve the action of the lower court in eliminating from the rate base certain leases as not used and useful, but included all the leases at their book value, adopting that figure for the reason that the company in question had not established any other value which was not purely speculative. The book value which the court adopted was not the original cost, such as was used by the court below for the leases of the Cities Service Gas Company on the authority of this case, but was a book value which the utility itself had placed upon its leaseholds. This value was accepted by this court as an admission against interest which in the absence of proper evidence as to present value prevented the utility from saying that its gas lands and leaseholds were being confiscated by the orders under consideration. The book value so accepted by this court was several times the original cost of the leaseholds.

We submit that none of the authorities cited in appellant's brief authorizies the exclusion of the leases which the Commission in this case excluded, or authorizes the elimination from the rate base at the present value of $12,000,000.00 found by the court below.

Hypothetical Pipe Line.

In order to meet the contention that was suggested during the course of the proceeding before the Commission that by reason of the fact the present system of the Cities Service Gas Company grew up out of the association and interconnection of previously unrelated pipe lines and was not designed and constructed as a single project, and that the system was larger than was necessary and contained duplications which would add to its value without being essential to service, the companies interested employed Ford, Bacon & Davis, Inc., a nationally known firm of engineers, to design and estimate the cost of a system which would serve the markets of the present company. These engineers, when employed, were instructed to estimate the cost of a line "as the crow flies rather than taking the actual topography into consideration," that the lines be designed as cheaply as could be done and on the assumption that the requisite gas reserves could be purchased without cornering the market.

George J. Rhodes, vice president and chief engineer of Ford, Bacon & Davis, testified as to the results of the study made by these engineers, and stated that the lowest figure for such a project was $91,500,000.00. The testimony of Mr. Rhodes is abstracted in the record at pages 333 to 338.

In their brief at page 140 counsel for appellant state:

> "The Commission upon consideration of the evidence pertaining to the hypothetical line was of the opinion it should be given no weight because in preparing the hypothetical pipe line no consideration was given to the fact that 50 per cent of the pipe line company's supply of gas was obtained in Kansas and Oklahoma, near the market, and because of the failure to give consideration to local gas."

We desire the Court to understand, in order that it may fully appreciate the consideration which should be given to this testimony, that these engineers were not employed to make a guess or an unfounded estimate based on general information as to what it would cost to build such a system and supply it with adequate gas reserves, but was employed to design and estimate the system with the same detail and accuracy as if the system was to be built and Ford, Bacon & Davis, Inc., intended to contract its construction. The Commission, as shown by the above quotation, gave this evidence little, if any, consideration, although its importance from the point of view of the companies is well illustrated by the fact that they paid these engineers $16,444.16 for their services and the time and detailed work which their study made necessary.

Counsel for appellant state that the evidence in regard to this hypothetical line was given little consideration because of the fact that it did not take into consideration the many gas fields in Kansas and Oklahoma. This is a strange contention in view of the fact that the Commission reduced the allowance for lease value by finding that gas reserves in Texas were sufficient for the requirements of the company for many years without drawing on the Kansas or Oklahoma acreage. The engineers employed were instructed to build the line to Texas for the reason that in no other place could it even be assumed that sufficient gas reserves could be acquired. That the gas in Kansas to which the system is connected is essential to service is evidenced by the fact appearing in the record that at intervals the pipe line to Texas has been out of service, due to breaks in the line, but that such interruption was unknown to customers on account of the fact that the supply in Kansas and elsewhere was sufficient to bridge over the emergencies. It must be apparent to

the court that if this hypothetical pipe line had been designed to connect with all existing gas fields to which the present line is connected, the cost would have been infinitely greater. Yet the fact that it is not so connected seems to be the sole basis for the contention of counsel that this evidence is entitled to no weight. It is not contended by counsel in support of this argument that the gas fields in Kansas are sufficient, as the fact that they are not cannot be disputed. If then they are not sufficient, the hypothetical line would, of necessity, have to be connected with the Texas field or some other field which would supply the deficiency.

Rhodes testified in connection with the hypothetical line that it would not render the service of the present system of the Cities Service Gas Company for the reason that it consisted of one line to each of the markets and was connected to but one field, which would not give the guarantee against interruption of service which now exists by reason of the inter-connection of the pipe lines of the present system served from many different fields.

When the above outlined facts are taken into consideration, we insist most earnestly that this evidence was entitled to, and should have been given great weight, instead of having been ignored.

Counsel states that there was no occasion for the construction of two 24-inch lines to the Texas field,

> "—in view of the fact that the company had a large amount of local gas available in Kansas and Oklahoma. This hypothetical pipe line covers a different plant and a different system and was more expensive to construct because the engineer in his estimate went farther than necessary to obtain the gas."

This argument was entirely without the record, no witness having testified that any such thing was true and

it being apparent from the contentions of the Commission itself that no adequate supply of gas for the system could be procured from any field other than that in Texas. It is very true that there is gas in Kansas and Oklahoma which is connected with the present system; but it is absolutely untrue that that supply is adequate or that any other line could be thought of or constructed which would serve the present markets with an adequate supply of gas at a less cost than that estimated by Ford, Bacon & Davis.

Assigned Error Number 5.

Present Values and Prudent Investment.

Under this assignment of error, counsel for appellant take exception to the finding of the court below that

> "The present values are on the extensive constructions of the last few years, less than the prudent investment therein."

The argument in support of this contention is based on two propositions: One, that a comparison of company costs and engineer's estimates on the construction of the Wichita-Ottawa 20-inch line does not bear out the court's finding; and the other, that there was a write-up of over $9,148,627.00 in the case of the Kansas Natural Gas Company.

We may be unduly dignifying the argument in regard to the construction costs of the Wichita-Ottawa 20-inch line by replying to it at all, for it must be apparent to anyone that one line out of the many involved in the system cannot be selected as the basis for any such comparison. We do not know why this particular line was selected.

Perhaps it was for the reason that the contractor, as he testified, on this line lost $128,000.00 over the actual cost of the labor on the line to him. The figures which counsel use as showing the cost of this line to the company are stated to have been made from an analysis of job order No. 12,145. We have, under another chapter of this brief dealing with right of way, shown that job orders do not represent actual cost to the company and contain none of the expense occasioned by the land and lease department, the legal department, the geological department, or any other than the construction department; or overheads which are otherwise capitalized. In addition to these objections, we might add that the job order is not in the record before this Court, and there is nothing in the record to show that any of the purported figures are correct.

The second argument of counsel is, that there is a write-up in the plant and investment account of the Kansas Natural Gas Company of $9,148,627.00. Counsel state that this write-up appears in Exhibit 9 introduced before the court. This is outside of the record, Exhibit 9 not being included in the record herein. And there was no evidence before the Commission or the court below that if any such write-up occurred in the plant account of the old Kansas Natural Gas Company before its acquisition by the present owners and consolidation with the present companies now comprising the system, it was carried into the plant and investment account of the present company.

Counsel state in their brief at page 146

> "That the total plant investment and other assets including leases is $95,948,321.00."

Counsel attempt to disprove the finding of the court by deducting from this admitted figure obtained from the books of the company the item of claimed write-up which they have not proven and which is not in the record before this Court and which applied to a predecessor company, and have then attempted to depreciate the resulting figure for the purpose of showing a less figure than that found by the court.

The finding of the court below is, that the actual prudent investment of the company in these properties was greater than the reproduction cost new depreciated value which the court found. The court did not find that the prudent investment depreciated was greater than present value, but merely that the prudent investment was greater than such value and this statement is borne out by the argument of counsel.

Assigned Error No. 6.

Conclusion As to Valuation.

Under this heading counsel for appellant have called attention to an error of $1,011,392.00 in the Commission's valuation, which correction we have accepted and applied to the valuation elsewhere in this brief.

The statement is made that although the valuation was made by the engineers in the summer of 1931, they did not use depressed prices then prevailing. The only thing cited in support of this statement is the quoted testimony of Black, to the effect that in making his appraisal, it was not his idea to use rock bottom prices of labor or material. There is nothing in the record to show that Hamilton did not use prices existing at that time and he has, as a matter of fact, done so. What prices Black

used we do not know, but evidently they were prices below anything anyone had ever known, for the Commission itself, in many instances, raised him thousands of dollars, and they are shown by the record to have been below the actual quotations received by Hamilton from manufacturers and used by him in his valuation, such prices being as of September 1, 1931.

The conclusion that Black was below normal prices is also evidenced by the fact that his valuation in almost every instance was lower than the actual cost to the company of the item priced, as we have hereinbefore set out with respect to the cost of drilling wells and constructing compressor stations. The court below recognized this situation when it stated in its opinion: "The Commission's figures are so far below the cost of these wells or any other well in the vicinity, that they approach the arbitrary." (R. 305.) The Commission in each instance adopted Black's figure or increased it, so that the above comment of the court is equally applicable to Black's valuation.

Our conclusion of value is that there should be added to the value which the court found, $82,380,583.00, the sum of $1,102,500.00 by reason of the failure of the court to apply agreed overheads to the cost of the leases found by it, if cost is the proper method of valuation, or the sum of $2,310,000.00 if such overheads should be applied to the present value of leases, which the court found to be $12,000,000.00. This would leave the valuation found by the court adjusted to correct this error either $83,483,083.00 or $90,963,311.00.

Rate Base During Each Annual Test Period.

Counsel for appellant said that the test period used in the investigation covered the years 1930 to June 30, 1932, leaving the impression that this was a test period agreed to by appellees. This is not true and the appellees never took any position other than that the reasonableness of the contract under consideration was to be determined as of the date of the hearing, and on the then experience of the company. It was agreed by the parties that the valuation should be made by the engineers as of September 1, 1931, and the Commission in the beginning requested the appellees to furnish an exhibit showing their financial experience for the last available period, which was June 30, 1931. The hearing having dragged out through the year 1931, on the request of the Commission the appellees furnished a further exhibit showing their experience for the year ending December 31, 1931, and, on rehearing, brought their experience up to date by an exhibit covering the period ending June 30, 1932. The reason the last two exhibits were furnished by appellees was for the purpose of showing their experience at the time of the hearing, it never being conceded by the appellees that it was proper for the Commission to take into consideration anything other than existing conditions.

For the purposes of this suit the appellees have consented to the application of its earnings for the year ending June 30, 1932, to the value found as of the agreed date of September 1, 1931, although it is apparent that such practice was to the disadvantage of appellees for if an accurate figure is to be arrived at as to rate of return, there would have to be included in the valuation of September 1, 1931, the additions and betterments since that date. This was not done because of the delay and expense involved and because, from appellees' viewpoint,

the earnings for the year ending June 30, 1932, showed the contract in question to be reasonable when applied to the valuation of the property in existence the previous year.

At no time during the hearings held by the Commission was any suggestion or intimation given by it or its attorneys, that it proposed to average earnings and average values over a period of years, and we are confident that such an idea did not occur to the Commission until, on its own findings, it came to the conclusion that the earnings for the last available period, when applied to the lowest value the Commission could find of the property, were still reasonable. It then resorted to the expedient of averaging earnings and averaging values, and arrived at the erroneous conclusions set out in its original opinion.

The figures which the Commission has used in undertaking to establish average values and average earnings are obtained from an exhibit which was introduced by its accountant, the purpose of which at the time was to support the Commission's contention that it was improper to apply the earnings of December 31, 1931, to the value of September 1, 1931, for the reason that such earnings came from only a portion of the property represented by the plant account, due to the fact that some of the property had been built within that year and while it appeared in the valuation, had not been in existence for the full year covered by the earnings statement. Appellees introduced evidence to show that this exhibit was entirely erroneous for the reason that it had been made up from the books whereas job orders frequently were held open for a year or two after the property was actually placed in operation before being charged into the books. This testimony appears in the record at pages 517 to 528 inclusive. It

is our contention that the exhibit from which these computations are made is entirely erroneous and not dependable. Had appellees known or had any reason to suspect that the Commission intended to use that exhibit for the purpose of averaging earnings and averaging values, the facts would have been shown but, even on the record as it exists, this method of arriving at average earnings is discredited.

We desire again to emphasize that the appellees at no time consented to any such thing or were given any opportunity to show the errors in the Commission's figures. The contention of the appellees before the Commission was and now is that if the Commission had any jurisdiction whatever, it was limited to ascertaining the present reasonableness of the contract on present values and the present experience of the company.

In support of their contention that it is proper to average earnings and average values, counsel quote from the opinion of the court below, in which it is stated "We agree with the Commission that 1932 should not be taken as a test year, for it marks, it is hoped, the low of the depression through which we are passing." That statement was made by the court almost a year ago and we regret to comment that the hope expressed by the court has not been realized and that, in fact, the low of the depression, if it has yet been reached, came long after the court's opinion was rendered. This merely demonstrates the danger of attempting to base a rate on hope instead of experience.

The depression has not passed, or even indicated that its demise is "just around the corner" as it was supposed to be some years ago. The business charts of today show little if any increase in the gas business, but do show greatly increased expense in holding the old busi-

ness, due to the NRA and the avowed policy of the present administration to increase labor and commodity prices, other than the commodity which public utilities happen to have for sale.

It is impossible for appellees to answer properly the labored and involved argument set forth under this heading for the reason that there is no record upon which the argument can be based and no record upon which the contentions can be answered.

The whole argument is based on the assertion that the test period used in the present investigation covered the years 1930 to June 30, 1932. As we have attempted to set out under the previous heading, there was no such test period ever agreed upon, and appellees had no reason even to suspect that any such contentions as are now made would be made.

The further statement is made that earning statements were submitted for yearly periods as follows:

> Year ending December 31, 1930;
> Year ending December 31, 1931;
> Year ending June 30, 1931;
> Year ending June 30, 1932.

It may be true that an exhibit was before the Commission setting forth the results of an investigation of job orders made by the accountant for the Commission as to these periods; but the inference that these statements were submitted by appellees or that appellees consented to their being considered in determining average investments is absolutely untrue. We have reason now to believe that this exhibit was not introduced by the Commission for the announced purpose, but for the express purpose of enabling it to avoid the obvious result of ap-

plying the then present earnings to the then present value. Appellees had no intimation that any such thing was to be done, and no opportunity to meet any such issue. Since the latter exhibit did not show any improvement in earnings or any improvement in the rate of return, the appellees took it for granted that the Commission would not attempt to change the date certain on which their finding was to be based.

The statement next made in appellant's brief is:

> "From findings of the Commission, it appears that the anticipated test period when the investigation was started was the year ending December 31, 1930, and the year ending June 30, 1931."

This statement of counsel was evidently made inadvertently, for it is an admission of all that we have heretofore said with respect to our never having agreed to averaging earnings or values over a period of years, but that it was intended at the time by all parties that the earnings of the company for the last available annual period should be taken as the measure of the reasonableness of such earnings.

The next argument of counsel for appellant is, that the books of the company showed an increase in plant and investment of $46,000,000.00 since November 30, 1926. If appellant desires to base the determination of this controversy upon the plant investment as shown by the books of the company, we are perfectly willing to submit the case on that basis; but, having repeatedly stated that they were not, we submit that no such argument should now be made.

Counsel proceed with the argument:

> "It is obvious that a comparison of net income during 1930 with the value of property used and useful as of September 1, 1931, would furnish no indication of the net return earned during 1930 on the value of the property used and useful during that year, as large additions were made to the property currently during all of that period as well as during the period from December 31, 1930, to September 1, 1931."

We do not see how this argument concerns the present consideration except as it admits the statement which we have repeatedly hereinbefore made that we have given the Commission an advantage to which it is not entitled in applying the earnings of the company as of June 30, 1932, to the value of September 1, 1931, for the reason that all additions since September 1, 1931, are eliminated. If there should be included additions since September 1, 1931, the application of present earnings to present values would be much more advantageous to the contention of appellees than the contentions we have hereinbefore made.

The remaining argument of counsel for appellant is based entirely upon the correctness of the exhibit from which the Commission attempted to determine the value of property in use at a certain period and the earnings of that period. As we have heretofore set out, the exhibit upon which the Commission based its findings was predicated upon the plant account as shown by the books whereas under the practice of the company job orders were not closed into plant and investment account until all of the claims and law suits arising out of that construction work had been settled, which usually required one to three years. The court below saw clearly that

this was true, and in the quotations from the opinion which appear in appellant's brief states:

> "—but this (the conclusion from job orders as to what property was in service at a particular time) is shown to be inaccurate because additions were not charged to capital until long after the addition was in service; a lag of some one to three years was customary in order to close up all claims growing out of a particular job."

We submit that in determining the present reasonableness of a contract, the entire procedure of the Commission was unwarranted, even if based upon dependable facts, and that these basic facts having been shown to be erroneous as found by the court below, no consideration should be given to any such yard stick for the measure of present reasonableness.

Net Income Before Depreciation and Depletion.

There is nothing in the argument under this heading other than a repetition of the argument previously made that it was proper to average earnings. We believe we have fully answered this contention elsewhere in this brief.

We might, however, call attention to the fact that counsel for appellant state that the only evidence justifying any addition for amortization of rate expense was the fact that the Commission taxed $66,935.08 as costs for the distributing company respondents. We recall very distinctly that elsewhere in this brief the company has made no reference whatever to the Kansas statute and, as stated, that the Commission's jurisdiction was assumed under the authority of the Western Dis-

tributing Company case which was decided more than seven months after this proceeding was started. There is nothing in the Western Distributing Company case which authorizes the Commission to tax the cost of a proceeding to the parties thereto, and this reference to the fact that the Commission did so tax such costs shows very clearly that the Commission was, in fact, proceeding under the authority of the statute which gives it no such authority as it has assumed.

The cost of this proceeding to the Commission may have been the figure quoted, but the expense of producing the evidence which the Commission required was far in excess of that figure. In the opening statement to the Commission (R. 226) counsel for appellees stated that the expense incurred before the taking of evidence started amounted to between $150,000.00 and $200,000.00. Before the proceeding ended, the expense exceeded $250,000.00. Who is to pay this expense? If the distributing companies should charge it to their operating expenses, what is the chance of having such an item allowed in view of the attitude the Commission has taken throughout this proceeding and in view of the fact that proof was offered that they are not now earning a fair return? The distributing companies being faced with the calamity of having to pay 40 cents for gas at the city gate, and basing their rates on 30 cents, which, under the undisputed evidence would result in insolvency, put on all this evidence to justify the reasonableness of their contract knowing that they could not get an item of $250,000 allowed as an operating expense and a basis of increased rates, they requested the pipe line company to assume this obligation, which it did; and the expense is amortized over a period of years at the rate of $50,000.00 per year. The Commission found that by reason of affilia-

tions, all the companies concerned should be treated as one. If so, and it being apparent that someone has to pay this expense, it should, on the Commission's reasoning, be immaterial to it which pocket the money came out of, and this item should not have been eliminated.

We again submit that in determining the reasonableness of the contract under consideration, the earnings of the Cities Service Gas Company as agreed upon for the year ending June 30, 1932, should be adopted at the figures shown by the company's books and without deductions therefrom.

Annual Depreciation and Depletion Requirements.

Annual Depreciation.

As stated by counsel for appellant, the parties agreed on 2.96 per cent to be applied to the value of physical property of the Cities Service Gas Company other than leases as a proper allowance for annual depreciation.

We have no comments to make other than that this percentage should be applied to the value of the physical property found by this court.

Annual Depreciation for Years Covered by Earning Statement.

We have heretofore set out our contention that it is not proper to average values or average earnings, both for the reason that the method is wrong in determining the present reasonableness of a present contract, and for the reason that the basic figures used by the Commission in this computation are erroneous and that appellees were given no opportunity to demonstrate their error.

The question of proper reserve requirements is not a question of mathematics or of averages, but is a question of what is presently necessary under present conditions, and is a matter which is to be determined by the business judgment of those in charge of the property, as was held in the case of *Southwestern Bell Telephone Company* v. *City of Fort Smith,* 294 Fed. 102, wherein the court said:

> "While the city may prescribe rates for telephone service, it is not the owner of the telephone plant. The telephone company is the owner of the plant and operates it. Its officers and employees are charged with the responsibility of its operation. Their experience enables them to form a judgment with reference to the amount to be reserved for depreciation. Until the Interstate Commerce Commission through its investigation shows the amount reserved by the company to be excessive, prudence would dictate that the judgment of the company upon that point should be permitted to stand."

The only evidence introduced before the Commission or before the court below as to depreciation requirements was the testimony of Eastman in support of his exhibit No. 27 in which he set up reserves totaling $3,276,325.07, which the Commission cut to the unreasonable figure of $1,702,764.00 (R. 156). Eastman testified that in preparing the exhibit he consulted with officers of the company and that the figures which he set up in his exhibit represent the judgment of such officers, and in many instances are the actual figures taken from the books of the company. There was no attempt to contradict this evidence by any showing of bad faith, fraud, or imposition, or that the books of the company did not show such allowances actually set up thereon. In the absence of

such a showing, the judgment of the officers of the company should prevail, and certainly the presumption that these allowances are proper should not be overcome by any presumption of the correctness of results attained by the Commission in juggling figures in the manner attempted herein.

Assigned Errors Nos. 15 and 16.

Annual Depletion Requirements—Gas Leases. General Development Expense Capitalized.

The substance of the argument under this heading is that if the Commission was right in eliminating all leases which it did eliminate for the reason that they were not used and useful, then the company is not entitled to an allowance for carrying the leases not found to be used and useful. With this argument we have no quarrel, but we contend, as hereinbefore set forth, that the Commission had no right to substitute its judgment, unsupported by any operating experience on the part of any member of the Commission and unsupported by any evidence in the record before the Commission, for that of the officers of the company responsible for service as to used and useful leases. If we are correct in our contention, then the allowance by the court of $329,917.00 should be sustained; otherwise, it should not.

Counsel for the Commission argue that in the Commission's valuation there was allowed not only the cost of leases but in addition all expenses for geological investigation, scouting and other expenses in procuring said leases, and in addition to this there was included an enhanced value as of September 1, 1931, in the valuation which they have fixed as the fair market value of these

leases as of that date (App. brief 161). This statement is entirely erroneous, and is not supported by the record. If the Commission, as stated by counsel, placed in its valuation the leases which it did allow on the basis of fair market value, they certainly did not include any of these expenses. It may be that the company in its geological researches expended thousands of dollars in investigating a field, which investigation resulted in the purchase of a lease for $100.00 or in no purchases whatever. If it did purchase a lease, it is immaterial what it paid for it or what the preliminary expenses were. The Commission judged the value of the lease on the basis of what it could be sold for at the time of the hearing. Counsel's statement that the Commission allowed fair market value is entirely inconsistent with the statement that these other expenses were included, and is untrue. There is no duplication and could be none if the leases were valued, as the counsel state they were, on the basis of fair market value.

Amortization of Non-Producing Leases.

The argument of the appellants under this heading is based on the supposition that the inclusion of non-producing leases at their fair market value in the rate base and an allowance of a fair return on that item plus an inclusion in the operating expenses of the cost of amortizing these non-producing leases results in a duplication reflected in rates to the customer.

This assumption is erroneous as is clearly shown by a careful consideration of the situation. The ordinary gas lease runs for a period of ten years and covers an annual rental during each of these years prior to the

time when the leases are developed. After the lease has been developed, this annual rental is replaced by a percentage of the gas produced from said lease. The error in the assumptions of the counsel for the appellant is that they assume that a lease which originally ran for ten years and has only one year to run would have the same fair market value as a lease on the same property which has ten years to run. This is directly contrary to the facts.

When any man experienced in the purchase and sale of leases attempts to compute the fair market value of a particular lease, his opinion is at once influenced by the length of time in which he has to develop that lease, and he does give a much lower value to a lease with one year to run than he would to a lease with ten years to run.

The inclusion in the operating expenses for amortization of undeveloped leases is just an inclusion of the amount of depreciation that occurs in these leases which depreciation was taken into consideration by the witnesses in their determination of the now present fair market value, and its inclusion is in no way a duplication of the item which is included in fair return based on fair market value.

There is no more duplication in this situation than there is in the determination of the present fair value of a piece of pipe or a compressor and the inclusion at the same time of the depreciation allowance which is to cover the reduction between the reproduction cost new and the present value in that same item of property. We do not understand the purpose of counsel's argument, inasmuch as the court below agreed with their contention, although the court stated, "Accordingly, with hesitation, we disallow the item." It seems very clear to

us that both the court and the Commission were in error in their findings.

Dry Hole Expense.

The argument of counsel under this heading is answered as well as we could do so by the finding of the court below, which is as follows:

> "The Commission assumed that one dry hole a year would be all that would be suffered in an orderly development of this vast property. The actual expenditure in the test year was $174,747.74, a sum representing the cost of ten or eleven dry holes. The facts must govern. The company is not needlessly drilling dry holes, and geology has not reached the point where only one dry hole a year can reasonably be anticipated by a company owning nearly a million acres of prospective leases, scattered in three states and many fields."

The contention made by counsel is such as could be expected from those entirely unfamiliar with the operations of a gas company such as the Cities Service Gas Company and the action of the Commission can perhaps also be accounted for on that ground; however, these non-experts have no right to assume without evidence, and the court will note that no citation is made to the record in support of any of the contentions made, that the company is going to any unnecessary expense in drilling dry holes; the entire argument is based on the assumption that these dry holes are to be drilled as "wildcat wells" on unproven territory. The fact is entirely overlooked that many leases provide that they must be drilled within a definite time in order to hold the lease and when this is done, it

must be anticipated that some dry holes will result. The Commission has assumed that the Cities Service Gas Company has a supply of gas much in excess of its requirements and that it has had for a number of years. If this is true, it is ridiculous to assume that the company in 1930 spent $174,747.74 in a search for gas which it did not need.

The argument reverts to what we have hereinbefore stated, that the officers of the company are presumed to be operating in the most economical manner and are making no expenditures other than such as of necessity have to be made. Many dry holes are drilled in proven gas areas and the argument of counsel falls because it takes more than one point to outline a circle and a proven gas area is always outlined by dry holes drilled at the edge of that proven gas territory, as well as by the fact that there is nothing in the record to support the argument made.

Assigned Error No. 18.

Fair Rate of Rate Return.

We have, in a previous part of this brief, set out in full the evidence introduced before the Commission and the court below as to a proper rate of return, and in addition have quoted the Kansas statutes which prohibit cities of the second class from fixing rates for gas companies which will produce less than a return of at least 8 per cent and in cities of the first class prohibits a return of less than 10 per cent.

We believe our previous argument fully answers everything that is said by counsel under this heading so far as a proper rate of return is concerned.

Counsel attempt to avoid the undisputed evidence in the case and the Kansas statutes by arguing that the financial history of the company since 1926 indicates that its total assets have been increased to such an extent that its earnings must have been unreasonable. This argument is made without support of the record for nowhere does it appear that the increase in assets resulted from earnings either reasonable or unreasonable; nor does the record show any valuation for those previous years on which an assumption could be made that there were unreasonable earnings, but even if there was support for these contentions, they are beside the point for it has repeatedly been determined by this and every other court which has ever considered the question that past losses can not be recouped in present rates nor excessive past earnings be taken into account in determining a proper rate for the present.

Effect of Commission's Order on Income.

Under a previous heading, we have applied the stipulated decrease in earnings to the business of the company for the year ending June 30, 1932, and as no errors have been pointed out in our calculation, we submit that they are correct. Counsel appreciate this when they attempt to argue that if the 30c rate had been put in effect, the additional consumption of gas would be such as to increase the earnings stipulated for the year ending June 30, 1932, and that therefore, such earnings are not a proper basis for the determination of the future experience of the company.

If, under any circumstances, there could be any basis for such an argument which is based on pure guess

work and conjecture, there certainly can not be in a case where the Commission itself comes into court and confesses to the invalidity of the order passing this reduction on to the consumer.

As this case now stands, there is no order reducing rates to consumers and can be none until valuations are made of the properties of all of these companies and their financial experience determined, which is a situation that can not arise for years in the future. We fail to see how the counsel for the appellants can predicate an increase in the consumption of gas on the part of individual customers due to a reduction in the cost of gas to the distributing company which reduced cost of gas, by their own confession, is not passed on to the ultimate consumer.

Rate of Return Under Commission's 30c Order.

We have previously fully discussed the application of the Commission's order as applied to the experience of the company for the last available period, June 30, 1932, and have also answered the contention that the year 1932 was an abnormal year, not properly taken as a basis for probable future experience. Its abnormality, as we have pointed out, is that it did not include the increased expenses and the decreased earnings caused by the NRA codes and the policy of the present administration to increase labor prices and the prices of all commodities other than gas. We also desire to contradict the statement made that the court below in its finding, abandoned the original test period. The court adopted the only test period to which appellees ever agreed and gave the appellants the benefit of an unrealized hope that 1932 was the bottom of the depression.

Decreased Income, Due to Loss of Industrial Sales—Value of Domestic Service.

The entire argument under the heading is that the earnings of the company, as shown by the experiences for the year ending June 30th, 1932, were lower than can be expected in the immediate future by reason of the fact that the company has sustained a *temporary* loss in income due to the decrease in industrial sales. The further statement is made "that loss was caused by abnormal conditions, if abnormal they will improve in the future." This is another attempt to determine reasonableness on the base of hope instead of experience. We sincerely wish it could be established that "if abnormal they will improve in the future." At numerous times during recent years nationally known economists, financiers, and persons occupying positions of importance in the government, have stated that the bottom was reached and conditions were bound to improve. They did not. On the contrary they became worse. With counsel we hope that the bottom has been reached, but we know far less about the situation than those who predicted it had been reached some years ago.

We are now supposed to be arguing as to the reasonableness of the conclusion reached by the Commission in 1932. There certainly has been nothing in the subsequent experience to indicate that the position taken by the Commission, or by the court, was justified, and we certainly are not optimistic enough as to the future to base our conclusion, as to the present, on what the future may have in store for us.

It appears to us also that this argument of counsel for appellant is entirely out of order for the reason that the business of the Cities Service Gas Company is that of supplying the requirements of its domestic consumers.

The supply to industries is purely incidental and is entered into because service to domestic consumers could not otherwise be maintained. It requires at least one day to transport gas from Texas to the major markets of the system. It is a matter of common knowledge that drops in temperature, of as much as thirty or forty degrees, frequently occur. In order to meet these fluctuations it is essential to service that the pipe line company either have storage tanks near points of delivery, the cost of which would be prohibitive, from which to meet the demands on the system, or have some other means of having immediately available a sufficient amount of gas to meet the fluctuations in the demands of the domestic consumers. In order to meet this contingency all of the contracts for industrial gas contain a clause providing that service may be discontinued when the supply is necessary for domestic consumers, and the industrial consumers are required, by such contracts, to maintain other fuel which can immediately be substituted for gas. The industrial consumption in the major markets is such that within one hour millions of feet of gas can be immediately made available for domestic use, and experience in the past has shown that in the absence of such gas, service would have failed completely. Therefore, industrial business is not primarily sought, or kept, for the purpose of profit but as a guarantee to domestic service. The price at which industrial gas is sold is determined absolutely by the price of other fuels. Before industries can be interested in the use of gas as a fuel it must be shown that they can make a saving over coal or oil, consequently without regard to profit, and even if the company was merely trading dollars, it would still be essential that the industrial business be maintained. It therefore follows that the argument of counsel should be given no con-

sideration and the cases cited to the effect that one class of consumers should not be required to carry the burden of another class are not applicable.

Assigned Error No. 20.

Under this heading counsel for appellant make some statements which to us are most surprising. As we read the argument, counsel are attempting to make the point that in the beginning the appellees herein consented to the jurisdiction of the Commission to determine the reasonableness of the gate rate charged them by the pipe line company, but objected to the Commission making any finding as to the valuation or earnings of their separate properties.

It is impossible to answer this contention and confine ourselves to the record before the Court, for in preparing that record, we certainly did not have in mind that any such contention would be made or that an issue was presented as to what we thought about the proceeding in the beginning, or at any other time.

In order that the Court may understand what this situation was, we are intentionally going outside the record before this Court and referring to the record before the Commission and the court below, so that if this Court considers any of the things argued by counsel under this heading material, the Court may order up the further record to which we have herein made reference.

The first thing that occurred was the opening statement of counsel for the several distributing companies, in part as follows:

> "If the Commission please, at the outset we must confess some uncertainty and confusion as to the nature of this proceeding; the purpose of the Com-

mission; its jurisdiction and our duty. There has never before been anything of the kind attempted and there is no precedent to follow. For this reason and to avoid any uncertainty as to our contentions we have filed written appearances for the several respondents.

We say the proceeding is unusual in that we have here joined in one order and involved in one hearing separate and distinct properties in some one hundred and eighty cities and communities. Some of these properties have heretofore been involved in separate rate hearings and such hearings as to one property have taken weeks. The rates of each system must of necessity be based on the value of its property and its financial experience. The statutes contemplate separate hearings and provide for a review by the courts on the record as to that property, the venue being determined by the location of the property. It would lead to the utmost confusion, would thwart the purposes of the statute and would jeopardize the statutory and constitutional rights of these several respondents should they be expected to submit to a joint hearing involving the valuation and financial experience of one hundred and eighty properties, none of which is, in any manner, concerned with any other property. We therefore enter this proceeding with the definite contention that it is not a rate case as to any particular property and involves no consideration of the reasonableness or unreasonableness of their rates.

In coming before this Commission we do so doubtful of the legal rights of the Commission to compel us to incur this expense, doubtful of the legal right to fix an interstate rate in view of many decisions of the United States Supreme Court to the contrary, but realizing a duty to the public to answer our accusers and make all facts public.

We trust this Commission will hear our evidence with open minds and give to us in some measure the benefit of an honesty of purpose. We have naturally

been disturbed by articles that have appeared in the press, attributed to members of this body, from which, if true, it would appear the case has been prejudged and its issues determined against us in advance. If so, of course this proceeding is but a farce and an idle gesture. We hope, however, by our conduct in presenting it, to merit your fair and honest consideration."

This statement appears at page 226 of the record, and we have quoted two paragraphs from that page, and two from page 228, but request the Court to read the entire statement.

Before the taking of testimony was commenced, a further discussion was had before the Commission as to the nature of the proceedings, and the Commission's attention was called to the formal objections filed by the distributing companies which are set out in the record herein at page 27. In that discussion, the Commission's attention was called to the last paragraph of the order under which the proceedings were held, in which the following apears:

"* * * and adjustment made in this respect as to charges made to the consumers."

The Commisison was asked whether this meant that this proceeding was a rate case. The question was answered by Mr. Hatcher, attorney for the Commission, as follows:

"The only thing that we have in mind here is to investigate the reasonableness of those contracts. If it is then disclosed that they are unreasonable, it will then be necessary for the separate utility to come in and show cause why that rate should not be reduced and a reasonable part of the reduction passed on to the consumer. I think that is clear." (Transcript 28.)

In the course of further discussion, the following occurred:

> "Mr. Hatcher: You are not denying the jurisdiction of the Commission to enter into an investigation to determine the reasonableness of the holding company contracts? Let us get straight on it. You are not denying their jurisdiction?
>
> Mr. Garver: I am not denying their jurisdiction to investigate, no.
>
> Mr. Hatcher: And determine the reasonableness?
>
> Mr. Garver: To enforce its determination, there is a serious legal question there." (T. 29, 30.)
>
> * * * * * * * * *
>
> "Mr. Hatcher: Now as to the fixing of an interstate rate, I would like to make this statement, that it is not our intention that the Commission will fix an interstate rate for the interstate pipe line, but we will examine into the reasonableness of that rate, for the purpose of determining the reasonableness of the contract; that is, that the reasonableness of that contract will be measured to some extent, that will be one of the tests, what is the return of the holding company, or the pipe line company. In no case will we attempt to fix a rate for the interestate pipe line, but it is one of the tests that we will use in this case." (T. 30, 31.)

At this stage of the proceedings, in spite of the persistent efforts of counsel to find out just what the Commission was proposing to do, they had succeeded in eliciting nothing more definite than the statement that the Commission was making an investigation of contracts, without any commitment as to what the Commission proposed to do at the end of the proceeding. After considerable testimony had been introduced, a motion was made by the respondents to dismiss the proceeding and end the expense on the testimony of the State's own

experts that the city gate rate was reasonable. This motion was denied by the Commission, its decision being announced by Commissioner Hill, in which he said in part:

> "It may be true, too, that the distributing companies are in the position to oppose any rate reduction that might result, if one could result, as a result of this hearing, but that is a matter that the Commission would have to determine after knowing more about the valuations of the distributing companies."

After the further introduction of testimony as to leases, and the value testified to by the witnesses for the Commission was added to the value of the physical property as testified to by Black, a motion to dismiss the proceeding on the ground that on admitted figures the pipe line company was not making earnings equivalent to 8 per cent for return and 4 per cent for depreciation requirements was made, which was overruled by the Commission as follows:

> "Commisioner Hill: Personally, I think, speaking for myself as one commissioner, it would be an unconscionable decision if at this time and under the present conditions, this commission would permit a return of 8 and 4. For that reason this motion is overruled.
>
> Mr. Garver: That is a very strange statement for somebody to make who is passing impartially on a lawsuit, to say you have your mind made up, to say that would be unconscionable. I am frank to say I cannot understand such a statement." (T. 2000, 2001.)

As the proceeding neared its close, the appellees became suspicious as to the real intention of the Commission and

began to doubt the frankness of its statement that the proceeding did not involve rates to local consumers or that the Commission had changed its ideas as previously announced. Therefore, the distributing companies produced witnesses, had them sworn, and proceeded to show the value of the properties of the distributing companies respectively, and their respective earnings as well as the value of their properties in the aggregate and their aggregate earnings. To this offer of testimony, attorneys for the Commission objected, which objection was by the Commission sustained. In regard to this offer of testimony and the ruling of the Commission thereon, the record below is as follows:

> "Mr. Welch: I would like to add, the only way we can go into that is like we have done with the other properties. It would take a valuation of these distributing plants which the company claims is worth $15,000,000, it would also require an investigation of their earnings, to see whether or not we agree with the claim that they are only making 4.6 per cent on that amount of money, and in order to make worth anything to the Commission at all, it would be necessary for us to make a valuation of this property, go into the question of their earnings, and that we are not prepared to do. It is not germane to this investigation, and I am giving that as an additional reason why the objection should be sustained.
>
> Mr. Garver: There is just one feature of the order which started this investigation, which caused me to put in that testimony, and that is the provision of the order which recites that all of these distributing companies are cited to appear here, and show cause why these contracts should not be revised if found to be unreasonable, and the last line of the order is, '. . . and such reduction passed on to the consumer.' Now it is our position, as I stated in the beginning, that the only way to determine proper rates of each

of these companies is to have a separate rate case as to each one, each company must stand on its own bottom, but where the reasonableness of the inter-company relations is brought into effect and where the Commission wants to know and cites us to show it should not be passed on to the consumer, then I think that we are called on to show the earnings of the distributing companies at the present time are only 4½ per cent and even if there was a reduction made of the City gate rate, it could not be passed on to the public.

Mr. Hatcher: We are not taking the position here, are we, or are you, Judge, that the over-all picture shows a decrease in rates? There may need to be reductions in some places, they would have to be treated separately, and the way this evidence has gone in, it has gone in collectively.

Mr. Garver: Each one must be treated separately, and there must be a separate case as to each one. I have no means of knowing what the Commission has in its mind other than reading its order. It was that provision of the order which caused us to object in the beginning to any rate case as to the separate companies involved in one proceeding.

Mr. Hatcher: We are taking the position this is only an investigation into the reasonableness of these contracts.

Mr. Stone: Isn't it fair to ask what sort of an order would be suggested, as counsel on the other side knows, in case it was found 40 cents should not be allowed, what would be the nature of the order that would be entered? Would it affect each distributing company, or would there then be a hearing as to the value of these properties?

Mr. Hatcher: I would not care to answer that, further than to say I do not think it would reflect the over-all picture, such as this testimony does.

Mr. Garver: If the Commission, in this case, does not intend to make any order as to the rates to consumers in individual distribution companies, this

should be stricken out. If the Commission takes the position that it is going to contemplate any such action, then it should remain in.

Commissioner Hill: If the Commission should find that a reasonable rate were 45 cents, we could not, I take it, in this investigation—

Mr. Garver: Then the only way to do would be for us, if we wanted to change the rates, to go through the statutory procedure for changing them.

Commissioner Hill: If it were found it was a reasonable rate, at the gate, that would be a finding that would be proper, and then there might be an order to the distributing company to show cause why they should not be put into effect, as I view it.

Mr. Stone: Would they be foreclosed on that question—your distributing company would then be foreclosed on the question of whether there was—whether 30 or 40 or 45 cents was a reasonable rate. You might start from there with the investigation. In other words, Mr. Hill, to be perfectly frank, suppose a blanket order is made, saying 40 cents is not reasonable and 30 cents would be reasonable, and then there would be a hearing as to a particular company as to whether its rates should be reduced, would that company be foreclosed or would it amount to an adjudication against that company on that point.

Mr. Hatcher: Was that your point?

Mr. Stone: Until an order is made, how could we appeal, because this blanket order applies to no distributing company, until application is made under it.

Mr. Hatcher: It would apply to it if they were paying too much for gas, the contract is unreasonable, and if a reduction should be decided on, they are paying 5 cents or 10, or 15 cents too much.

Mr. Stone: But it cannot go into court and contest that order, until it is shown it affects its rates and confiscates its property.

Mr. Hatcher: I think any one of them or all of them could, because we have said the contract is unreasonable.

Mr. Garver: I want the record to show I am offering this testimony, by reason of the fact of the order which cites us to show cause why if a rate reduction is made, it should not be passed on to the consumer.

Mr. Hatcher: It is my idea that the companies would then have an opportunity to show whether or not, in a separate hearing, the reduction should be passed on.

Mr. Stone: Yes, but would they be foreclosed on the question of whether 40 cents was a reasonable rate or not?

Mr. Hatcher: Absolutely.

Mr. Stone: Then if they would, it ought to go clear down the line as to the distributing companies, in order that they may—when that order is made, an appeal may be made to the courts.

Mr. Hatcher: The distributing company is the only one in justifying this contract.

Mr. Stone: Our property is not confiscated until a reduction order is made.

Commissioner Hill: There are three points involved in the investigation. The 1¾ per cent fee, the 5 per cent fee and the reasonableness of the rate at the city gates, charged by the main lines. If we opened the hearing, or proceeded upon the theory now that we would investigate the reasonableness of the rate as it applied to each distributing company, as suggested by counsel for the state, there would have to be an appraisal and valuation of each distributing company's property, I think, under the scope of the investigation, the objection should be sustained and that the testimony should be stricken out.

Mr. Garver: We are offering to show, under the terms of the order that cites us to show cause why the reduction, if made, should not be passed on to

the distributing companies, that they, as a whole, are earning only 4.6 per cent, and that each company as this time is making less than it is entitled to earn on the present fair value of its property, and that considering the property as a whole, and assuming that it is all owned by the Cities Service Company, both the pipe line and distributing companies, that the entire properties are not earning a fair return at this time.

* * * * * * * * * *

Mr. Garver: If the Commission is contemplating passing this reduction, or passing any reduction on to the distributing companies, we now formally demand a separate hearing for each distributing company, a separate docketing of each case, separate and distinct from all others, and a hearing as to the valuation and financial experience of the several companies.

Mr. Hatcher: That is a question to take up after the Commission makes an order.

Mr. Garver: Counsel has just said we would be estopped after your order is made, to dispute it.

Mr. Hatcher: You do not have to open up this same hearing again in each one of the plants.

Mr. Stone: We want it in the record in each case, we will show in each case, it may not be as a part of the record.

Commissioner Hill: You would probably offer it if there were other hearings.

Mr. Stone: Yes, but he says we are estopped by the order, and therefore we cannot question it and there is no appeal to take from a blanket order.

Mr. Hatcher: It is my idea, the order will be only as to the reasonableness of these contracts, and the Commission has a right to investigate any single property of any utility.

Commissioner Hill: The objection will be sustained." (T. 2857-2864.)

From these excerpts from the record, this court must now clearly understand that the appellees during all the time they were before the Commission had no distinct idea as to what the Commission intended to do or what they were called upon to do to protect their rights. In the face of repeated statements of counsel and Commissioners to the contrary, this proceeding ended in the order of July 20, 1932, in which the Commission found that any rate for gas at the city gate in excess of 29.5 cents was unreasonable, and mandatorily ordered the distributing companies to immediately reduce their rates to local consumers so as to pass on the difference between purchased gas at 40 cents and 29.5 cents. The court will note that but one order was issued at that time.

After the application for rehearing was filed, which appears in the record at page 29, and after the argument of counsel for appellees on the rehearing granted, evidently the Commission itself became extremely skeptical as to the validity of the order it had previously issued, and in despair grasped at the expedient of issuing two orders, which it did on August 31, 1932, being the orders in controversy herein.

We have set out the foregoing record in some detail in order that this court may clearly see the unfairness of appellant in attempting to argue that appellees changed their position before the Commission with respect to its jurisdiction. As a matter of fact, the appellees never knew where they were and never had any position. They tried their best to pin the Commission down to some statement as to what it proposed to do, and as a result of their efforts were repeatedly told that the case was not a rate case. Notwithstanding all this, the Commission deliberately did just the thing it

said it did not propose to do. It made an order affecting local rates, after saying it would not do so, and after repeatedly refusing to hear the evidence offered by appellees as to the value of their respective properties and their operating experience. It seems to us that appellant is in a poor position to now argue that appellees are guilty of any vacillation.

Conclusion.

We respectively submit:

1. That the Public Service Commission of the state of Kansas was without jurisdiction or authority to issue the order for investigation set out in Exhibit "A" to the bill of complaint in the court below (R. 25), or to conduct the hearings which it did conduct thereunder.

2. That the two orders issued by the Commission under date of August 31, 1932 (R. 59-62), should be considered as one order establishing rates to local consumers, and that upon confession by appellant that the part of such order which established local rates was void the entire order should have been permanently enjoined.

3. That there is no justiciable issue now before this Court, and the decision of the court below should be affirmed for the reason that all issues are now moot.

4. That the reasonableness of the day to day contract between the Cities Service Gas Company and the several appellees herein respectively under which gas is purchased at the city gate should be determined on present values and present operating experience, and not by the consideration of undependable average values, average

earnings and average replacement reserves as was done by the Commission.

5. That on the admitted facts the earnings of the Cities Service Gas Company under its said contract are reasonable and should have been so found by the Commission.

6. That no examination by this Court as to the value of the property of the Cities Service Gas Company or its earnings is necessary or proper herein for the reason that on the admitted facts the contract of the Cities Service Gas Company is a reasonable contract unaffected by the affiliation of the parties, and such a contract as parties dealing at arms' length would have entered into.

7. That the findings of the court below, if value is in issue herein, are supported by the overwhelming weight of evidence.

8. That the decision of the court below should be affirmed.

Respectfully submitted,

ROBERT D. GARVER,
Kansas City, Missouri.

ROBERT STONE,
Topeka, Kansas.

SUPPLEMENTAL BRIEF

In the Supreme Court of the United States

October Term, 1933.

THE STATE CORPORATION COMMISSION FOR THE STATE OF KANSAS, HOMER HOCH, JESSE W. GREENLEAF, ET AL., *Appellants,*

vs.

THE WICHITA GAS COMPANY, THE HUTCHINSON GAS COMPANY, THE NEWTON GAS COMPANY, ET AL., *Appellees.*

Appeal from the District Court of the United States for the District of Kansas.

No. 114.

SUPPLEMENTAL BRIEF OF APPELLEES ON QUESTIONS OF JURISDICTION ARISING ON ORAL ARGUMENT.

In view of the fact that attorneys for the appellant during oral argument and in answer to questions by the Court stated that the appellant did not now take the position that appellees were estopped at any time and in any subsequent proceedings to have reviewed by the

courts the reasonableness or legality of the orders of the Kansas Commission of August 31, 1932, and that said orders were at all times open to judicial review if attempted to be enforced, appellees requested the Court for an opportunity to file this supplemental brief, the granting of which request is greatly appreciated.

Appellees were greatly surprised at the admissions made by counsel to the effect that the Commission did not now claim any of the orders made by it in this proceeding were of any binding effect upon anyone, or were other than preliminary steps taken in a proceeding the purpose of which was to ascertain rates; and this contention being the opposite of any contention theretofore made, appellees naturally did not discuss the matter in their original brief.

We understand the questions now presented are: Did the court below on the allegations of the bills have jurisdiction of the case as originally instituted? If so, was such jurisdiction defeated because of some concession made during the progress of the case? The bills by proper and substantial allegations presented a federal question. In a case in which the jurisdiction of the District Court is properly invoked upon a substantial controversy arising under the constittuion of the United States, the jurisdiction of that court and of this court of appeal extends to the determination of all questions involved, including questions of state law, irrespective of the disposition that may be made of the federal questions and whether it be found necessary to decide them at all. *Greene* v. *Louisville and Interurban Railroad Company,* 244 U. S. 499; and *Siler* v. *Louisville & Nashville Railroad Company,* 213 U. S. 175.

Jurisdiction of the court below.

Ten separate bills of complaint were filed by the ten distributing companies, appellees herein, all being in substantially the same form as the bill of complaint of the Wichita Gas Company, appearing in the Record at page 1.

In these bills of complaint it was alleged that the two orders of August 31, 1932, and each of them were

> "—unlawful, unreasonable, and void because in direct violation of the constitution and laws of the State of Kansas, and the constitution and laws of the United States, as hereinafter specified."

The orders were not alleged to be unconstitutional for one, but for many reasons, among which were that one order by its terms became effective immediately instead of thirty days from the making thereof; that the Commission made no finding as to the reasonableness of existing rates as required by Sections 66-110 and 66-113, Revised Statutes of Kansas, 1923 (R. 19); that the Commission did not fix any rates to be substituted for existing rates as required by Section 66-110 (P. 20); that the Commission undertook to fix rates without affording plaintiff its day in court or an opportunity to be heard (R. 20); that the rates established were confiscatory; that the Commission had no jurisdiction to act in the manner attempted (R. 21); and that in all these and many other respects the orders and each of them were void

> "—in that they deprive plaintiff of its property without due process of law; deny it the equal protection of the law; impair the obligation of its contracts; undertake to legislate with respect to interstate commerce and usurp the business management

> of the plaintiff company, all in violation of the constitution and laws of the United States and of the State of Kansas, and particularly Clause 3 of Section 8 of Article 1, the first sub-division of Section 10 of Article 1 of the constitution of the United States, and the 14th Amendment thereto." (R. 22.)

When under these bills of complaint the proceeding came on for hearing on plaintiff's application for a temporary injunction, attorneys for the Commission admitted that the order, Exhibit "M," was void for the reason that by its terms it became effective immediately instead of thirty days after the date it was issued.

No separate judgment or decree was entered upon the Commission's admission that Exhibit "M" was invalid, and the case was before the lower court until its final decree on all the issues raised by the pleadings except as modified by the Commission's admission.

During the course of the proceeding plaintiff offered evidence proving that if the distributing companies were required to pay 40 cents per M. C. F. for gas at their respective city gates and base their rates on a price of 30 cents per M. C. F., they would not even make their operating expenses. (R. 371.)

It is doubtful whether the orders or either of them were void because made immediately effective, as the statute does not prohibit the making of such an order, but merely defers its effective date. The statute, Section 66-115, R. S. 1923, is as follows:

> "*Effective date and reasonableness of orders.* All orders, regulations, practices, services, rates, fares, charges, classifications, tolls, and joint rates fixed by the commission shall be in force and effect on and after thirty days from the making thereof and expiration of thirty days after service aforesaid, shall

be *prima facie* reasonable unless, or until, changed or modified by the commission or in pursuance of proceedings instituted in court as provided in this act. (L. 1911, ch. 238, Sec. 18; May 22.)"

If the effective date of the order had been the sole ground for challenging its validity, the court could have well said the rates therein prescribed should be effective October 1, instead of September 1, and all objections would have been met.

The court below considered before it at all times all issues as to the validity of the orders on all of the grounds alleged, and made findings on the issues so raised, findings Nos. XX and XXI being as follows:

> "XX. If the distributing companies are compelled to pay 40 cents per thousand cubic feet for gas at the city gates, and to base their rates to the consumers upon the price fixed as reasonable by the Commission, no one of them will have earnings in excess of operating expenses, applicable to depreciation and return. (R. 319.)
>
> "XXI. The distributing companies could not continue their business and pay the Cities Service Gas Company 40 cents per thousand cubic feet, and predicate their rates to the consumers upon 30 cents; the Cities Service Gas Company could not continue its business without the patronage of the distributing companies. (R. 319.)

Conclusions of law were made on the above and other findings, and the decree was based on the findings and conclusions and not on any attempted admission or confession.

In addition to the issues raised by reason of the allegations in the several bills of complaint that the orders in question deprived the plaintiffs of their property with-

out due process of law, denied them the equal protection of the law, impaired the obligation of their contracts and confiscated their property by reason of the rates attempted to be established therein, the issue was also presented to the court below as to finding No. 11 of the order of August 31, 1932 (Ex. "L," R. 59), which finding was as follows:

> "That the costs hereof incurred by the Commission herein, amounting to $66,936.08, should be taxed to and paid by the respondents."

In addition to this item of $66,936.08 taxed as costs by the Commission, the court in its finding under the heading, "Operating Income" (R. 314), in effect found that the appellees had been to an expense of $250,000.00 in the preparation and presentation of the case before the Commission.

The court below, therefore, had before it the issue as to whether the Kansas Commission could compel the appellees to pay this item of $66,936.08, and whether the Commission could in the manner attempted put the appellees to an additional expense of $250,000.00 without violating their constitutional rights.

It seems to us that if the Kansas Commission by reason of the above finding is endeavoring to compel plaintiffs to pay this large sum of money and is doing so unlawfully, it is confiscating plaintiffs' property just as truly as if rates were established which failed in that sum to produce a reasonable return.

The Kansas statute under which these costs were taxed, Chapter 240 of the Session Laws of Kansas of 1931, is as follows:

"Section 1. That whenever, upon any investigation of a public utility made by the public service commission, on its own initiative or upon complaint filed, the commission shall find that any rate, toll, charge or schedule or joint rate is unjust, unreasonable, excessive, insufficient or unjustly discriminatory or preferential or otherwise in violation of the public utility act; or that any measurement, regulation, practice, act or service is unjust, unreasonable, unsafe, insufficient, preferential or discriminatory or otherwise in violation of the public utility act; or it shall find that any service is inadequate or that any service that can reasonably be demanded is not being furnished; or when an investigation is necessary because of an application by a public utility and such application is not justified, the commission shall ascertain and declare and by order fix the expenses incurred by the commission upon such investigation and shall by such order direct such public utilities to pay to the state treasurer to reimburse the fund appropriated for the public service commission an amount to cover the expenses so incurred: *Provided,* That such order shall not become operative unless the matter in connection with which such investigation shall have been made shall have been finally determined, by appeal or otherwise, adversely to such public utility. The Commission shall cause a certified copy of all such orders to be delivered to an officer or agent of the public utility affected thereby, and all such orders shall, of their own force, take effect and become operative twenty days after final determination of the investigation by appeal or otherwise: *Provided,* That if appeal is taken by any public utility a surety bond shall be furnished by such utility to secure the payment of such expenses in case the order of the commission shall be sustained."

It will be noted that this statute provides that the order of the Commission taxing costs shall not become effective until the matter under investigation "shall have been finally determined, by appeal or otherwise, adversely to such public utility," and that all such orders shall become operative twenty days after final determination of the investigation by appeal or otherwise. If then, the appellees herein had not filed their several bills of complaint in the court below, the finding directing them to pay this $66,936.08 would have become conclusive and appellees would have been compelled to make payment.

It will be noted also that under this statute there must be a determination adverse to the public utility, and it follows that the court below (if it felt that Exhibit "L" should not fall by reason of the admitted invalidity of Exhibit "M") could not determine whether the appellees should be required to make this payment without first determining that the order requiring the payment was either illegal or unreasonable. Without regard to the matter of rates, the court had to do exactly what it did do in order to determine this issue.

It should be perfectly apparent that if appellees had not filed their several bills in the court below and sought the relief which they did seek, both the orders, Exhibit "M" and Exhibit "L," would have become effective; plaintiffs would have been required under the provisions of order, Exhibit "M," to put into effect rates which would not even return them their operating expenses, and would in all future rate cases have been met with the contention that the order, Exhibit "L," establishing a 30 cent city gate rate was conclusive and binding upon appellees and would have been compelled to pay $66,936.08 costs.

We are entirely unable to understand how it can be contended or even thought that the Commission could by admitting the invalidity of Exhibit "M" on one of the many grounds on which it was alleged to be illegal and unconstitutional divest the jurisdiction which the lower court clearly had at the time the several suits were filed. If at the time this admission of invalidity was made the court below had dismissed the bills of complaint for the reason that no further issues remained for its determination, the rates established for appellees in Exhibit "M" would not and could not have been enjoined but would have forthwith gone into effect, and appellees would have been compelled to pay the large sum of $66,936.08 thereby suffering confiscation of their property not only to the extent of the unreasonableness of the rates fixed, but to the extent of $66,936.08 in addition thereto. It is solely by reason of the decree below that these orders are not now in effect and if the case had been or should now be dismissed they would become effective.

We do not desire to go over matters discussed in our original brief, but desire again to earnestly call the attention of the Court to the fact that these two orders were originally one order, that of July 20, 1932; that there is no explanation now before this Court, nor has any been attempted, as to why two orders were issued instead of one on August 31, 1932; that the orders were not in fact made in good faith or for any proper or legitimate purpose, and should now be considered as one. If considered as one, the part of the order fixing rates was admitted by appellant to be invalid on one ground, and was found by the court to be invalid as to that ground and for the reason that it was confiscatory. This left

nothing but the order Exhibit "L" upon which the order establishing rates was based which should have fallen and been permanently enjoined as a part of one invalid order.

If the orders are to be considered as two separate and distinct orders, then the order Exhibit "M" establishing rates should be enjoined because the rates were confiscatory, and the order Exhibit "L" which found 30 cents to be a reasonable city gate rate should be enjoined for the reason that the Commission had no authority to make it and for the reason that included in it was the direction to appellees to pay $66,936.08, thereby confiscating their property to that extent. That the Commission had no authority to issue the original order calling companies operating in 135 cities before it except to establish local rates is clear from a reading of the statute, Chapter 239, Session Laws of 1931, quoted in our original brief at page 2. All authority for the Commission to act is purely statutory as it is a creature of the statute. Any attempted assumption of jurisdiction beyond that expressly conferred is void.

> "The maxim that a legislature may not delegate legislative power has some qualifications, as in the creation of municipalities, and also in the creation of administrative boards to apply to the myriad details of rate schedules the regulatory police power of the State. The latter qualification is made necessary in order that the legislative power may be effectively exercised. In creating such an administrative agency the legislature, to prevent its being a pure delegation of legislative power, must enjoin upon it a certain course of procedure and certain rules of decision in the performance of its function. It is a wholesome and necessary principle that such an agency must pursue the procedure and rules

enjoined and show a substantial compliance therewith to give validity to its action." *Wichita R. R.* v. *Public Util. Comm.*, 260 U. S. 48, 58.

The bifurcated order was an attempt to trick the distributing companies so that they would not be able to attack the order in court until the order reducing the 40 cent rate had become binding and in a sense *res adjudicata*. This was expressly and emphatically stated before the Commission as set out in our former brief at page 168, and was reaffirmed in the court below. The lower court said that this kind of a proceeding could not be tolerated. (R. 284.) If permitted to stand, this dual order would not only have bound the distributing companies as to the 30 cent gate rate order but would have immediately deprived them of their income by the overnight reduction of rates. There was no alternative for the companies except to defy the Commission, treat the whole proceeding as a nullity, or appeal to the courts for protection. The complaints were filed. To have taken the other horn of the dilemma and to have defied the Commission would have subjected the companies not only to severe pains and penalties but to proceedings for receivership which were openly threatened by the Governor of the State who had ordered the defendant Attorney General to institute court proceedings seeking dissolution of the several companies and asking the appointment of receivers. This is set out in the bill of complaint at page 22. This proposed prosecution which amounted to duress was widely advertised in the public press. It is also alleged in the bill that the plaintiffs would suffer irreparable injury; that the penalties provided for infraction of orders of the Commission are so enormous, cruel and unusual as to intimidate the plaintiff

and force it to abandon any rights it may have to act independently thereof; that the plaintiff would be unable to make collection from its consumers for gas sold and delivered to them if it attempted to act contrary to the orders in the absence of relief by the court. (R. 24.) These allegations gave the court jurisdiction. The orders had actually been promulgated and the threats had actually been proclaimed and published by the Governor and the Commission. We do not know how a better case for injunction could be stated than is found in these bills of complaint. After the restraining order had been issued and at the hearing for issuance of a temporary injuction, counsel for the Commission on September 24, 1932, appeared in open court and stated that the threatened receivership proceedings would not be filed and admitted that the second part of the bifurcated order was invalid because under the statutes of Kansas orders of the Commission fixing rates could not become effective within thirty days. This, however, was only a statement of counsel and there was no order of the Commission canceling or rescinding that portion of the order which was said to be invalid. The answer filed on October 3rd, however, contains an admission that the order, Exhibit "M," is unlawful and therefore void under the laws of the State of Kansas. (R. 255.) The jurisdiction of the court had already attached. A court of equity had already reached out its protecting arm to save the complainants from being subjected to the unlawful acts which were being threatened. Defendants could not rob the court of that jurisdiction by coming in and confessing that one of the facts alleged was true. The jurisdiction of a court cannot be taken away by any such confession of wrong-doing by the defendant. The confession only

confirms the jurisdiction and justifies a judgment in favor of the plaintiff and against the defendant.

In the case at bar, the defendants might have come in and said, "We did not issue the order or the order did in fact allow thirty days' time, or that all requirements in respect to its issuance had been complied with" but it did nothing of the sort. It admitted the issuance of the order and then admitted that the order should not have been issued. The court thereupon and after the hearing on the merits issued its injunction against both orders (R. 361) and justified its jurisdiction in the opinion. (R. 282.)

How is it possible for a defendant to defeat the court of jurisdiction which has once been lawfully acquired by merely dissolving the issue by a confession of some of the allegations of the petition? This to us seems unthinkable.

As stated in our former brief, it is our contention that upon announcement by counsel for the Commission and especially upon the filing of the answer, the court could and should have entered a permanent injunction and ended the case without the expense of further hearing. The case in that sense only therefore became a moot case because without it there was no rate order, but the case was not subject to dismissal and the court was not deprived of its jurisdiction. It may have done an unnecessary thing in proceeding with the lengthy hearing, but its decree when entered did not become invalid and of course should not be set aside by this court.

During argument as to the binding force of the first part of the order, finding that the city gate rate should be reduced from 40 cents to 30 cents, in open hearing before the Commission counsel for the Commission were pressed to an answer and there stated that it was the

contention of the Commission that an order reducing the city gate rate would be absolutely binding upon the distributing companies as soon as it had been in effect thirty days and was not appealed from or attacked in court. See our original brief, page 160. This same question was presented to counsel at the hearing before the three-judge court and the position of the Commission was again reiterated. Judge McDermott interrogated Mr. Hatcher particularly on this point and asked him almost the identical questions which were propounded to Hatcher and Welch by Justice Roberts at the hearing in this court, to-wit: whether it was the contention of counsel that a rate could be built up by making findings and orders respecting the several component elements of a rate and each order become successively binding upon the distributing companies so that when the final order was made only one single element, for instance, the rate of return, would be open to attack because each of the others had become successively binding. It was then stated as it was first stated in this court that such was the contention of the Commission. This called for the statement of Judge Phillips in his opinion (R. 283) where he says:

> "Had the distributing companies failed to appeal from such order or seek a judicial review thereof within thirty days from August 1, 1932, it would have become final on September 1, 1932 (Sec. 66118, R. S. Kan. 1923), and the facts therein found would have become *res adjudicata* and, in that event, at the hearing under the last paragraph of the second order, the companies could not have defended against an elimination of such items as a part of their operating cost in fixing their rates."

But now, at the oral argument in this court, counsel again shift their position because they recognize the *reductio ad absurdum*. They frankly admit, as did Mr. Welch, that it is their present position the order would not be binding and that they will not now contend it to be binding. This is inconsistent with the position formerly taken by them, not only in the hearing before the Commission but also before the trial court. Is it possible that by thus shifting around on these two issues, the Commission can finally win this lawsuit after compelling the distributing companies to resort to a court of equity for protection against the orders which the Commission had leveled at them, which the Commission then claimed were valid and binding orders and would become *res adjudicata*, but which they now say were invalid and ineffective and could not become binding until applied in a specific hearing as to each distributing company in which its property is valued, its net income analyzed, and proper rate of return determined? We quote from the lower court at page 283 as follows:

> "If the construction of counsel for the Commission is correct, the order is plainly an attempt to avoid a judicial review in this court of the matters therein determined, and to deprive the distributing companies of their constitutional rights. This cannot be tolerated."

As to appellant's contention in this court that order Exhibit "L" is merely a step in a rate case and not a final order and therefore not subject to injunction.

As we recall the statements made by counsel for appellant on oral argument it was contended that this whole proceeding was merely a step in the process of

rate making which the Commission intended to apply in the future if and when rates to consumers came under its consideration, and valuations and audits were made of the properties of the several appellees.

We contend the proceeding as instituted by the Commission was not a rate case both because of the caption of the proceeding, hereinafter quoted, and because it was not a proceeding to ascertain the reasonableness of a rate or charge to be made by any public utility which is the only proceeding authorized by the statute under which the Commission assumed to act. Throughout the entire proceeding the Commission insisted it was not a rate case, and on that ground excluded all evidence as to the value of the properties of the several operating utility companies and all evidence as to their operating experience. Nevertheless, upon the termination of the proceeding the Commission entered a rate order. Upon rehearing this order was split into two parts, one of which fixed a city gate rate applicable to all utility companies, Exhibit "L"; and the other fixed a rate to the ultimate consumer, Exhibit "M." Therefore, although the case was not instituted as a rate case or treated as such by the Commission throughout the long hearings before it, it ended as a rate case with the final orders above recited, each of which it was contended would be conclusive unless set aside by the courts as provided by the statutes.

At this point surely the appellees were entitled to recourse to the courts as to the order fixing a rate to the consumer which was claimed to be confiscatory; and likewise they were entitled to recourse to the courts as to the order which fixed a city gate rate.

Upon the hearing in the court below, the Commission admitted the invalidity of order Exhibit "M" and con-

sented that it be permanently enjoined. But this could not oust the court of jurisdiction originally obtained. On the Commission's own admission this injunction should stand. As to this branch of the case, the decision below is a judgment by consent, and therefore is not subject to review.

When the case reached this Court, the Commission again made a shift of position, this time with respect to the order fixing the city gate rate, Exhibit "L," reversing the position always taken below, and contended that such order was not final and binding or *res adjudicata*. But this last position cannot affect the situation except in the court below.

On the facts then before the court below, its injunction was proper and therefore its decree should be affirmed.

We have joined in this one proceeding before the Commission ten companies operating in 135 towns and communities, each separate and distinct from every other property, and all of the value of $15,326,298.00. (R. 7.)

There is no rate case pending as to any of these properties, and without the pendency of such a proceeding, the Commission was without any authority whatever to act. As pointed out in our original brief, the statute under which the Commission is proceeding (Original brief, page 2), gives the Commission authority to act only

> "—in ascertaining the reasonableness of a rate or charge to me made by a public utility."

It cannot be said that any public utility has a rate case by reason of this proceeding. The order instituting the

investigation cannot possibly be construed as an order instituting a rate case. The title of the proceeding is:

> "In the Matter of the Investigation of the Reasonableness of Contracts and Charges Made by Holding Companies to Subsidiary Companies of the Cities Service Company."

There is nothing whatever in the above language to indicate that the rates of any company were under investigation or that the Commission intended to fix the rates for any company. As pointed out in our original brief, pages 160 to 171, the Commission repeatedly stated it was not a rate case, and repeatedly refused to permit any of the appellees to show the value of their properties or their operating experience. Again before the court below when evidence was introduced as to the value of the properties of the several distributing companies and their operating experience, the Commission objected on the ground that it was not a rate case. (R. 371.) If it was not a rate case, as repeatedly stated, then the Commission had no authority to act and the whole proceeding is void and unconstitutional.

If under any possible theory the order issued by the Kansas Commission (R. 25), or the proceedings had before it, can be construed as a rate case for any particular property or company, then certainly the Commission could not lawfully or in good faith take the position that in that proceeding it could find 30 cents instead of 40 cents to be a reasonable city gate rate, and that unless the several companies involved sought a review in court of the reasonableness and legality of the Commission's finding, they would be forever and conclusively foreclosed, and all future rate proceedings

would start from the city gate rate so found. This is exactly the contention that was made before the Commission, and the contention that was made in the court below. On page 168 of our original brief, we have shown from the record exactly the position taken by the Commission:

> "Mr. Stone: Yes, but would they be forceclosed on the question of whether 40 cents was a reasonable rate or not?
> Mr. Hatcher: Absolutely."

This position was taken before the Commission, and the rulings of the Commission in refusing to hear evidence as to the value of the distributing company properties or their operating experience, and in refusing to give them their day in court as to their local rates, were all predicated on the finding of the Commission becoming absolute.

It is our contention that the proceeding before the Commission by the terms of the order instituting it was intended to be and was limited to the ascertainment of the prices which the several appellees should pay for gas at their respective city gates, and that it was not intended to be and could not, under the Kansas statutes, be merely a step in the process of arriving at rates for the several distributing companies. This proceeding was concluded by the issuance of the orders in controversy. Thereafter the Commission itself could not change such orders, and certainly counsel could not change them or their effect by any admissions they might make in court or elsewhere.

In the case of *State ex rel.* v. *Atchison, Topeka & Santa Fe Railway Company,* 109 Ks. 847, the syllabus by the court reads:

> "Mandamus — Utilities Commission — Changing Railroad Freight Rates — Notice of Hearing Required. The Public Utilities Commission cannot, by declaring that it retains jurisdiction of a matter in which it makes a complete order fixing railroad freight rates in response to an application pending before it, defeat the necessity of giving the thirty days' notice required by Section 8341 of the General Statutes of 1915, in a subsequent proceeding in the same matter to cancel the order first made."

The holding of this decision is, that even if the Commission retains jurisdiction, which it did not do in this case, it could not subsequently proceed to change any order previously made without giving the utility concerned thirty days' notice as required by the statute. There has been no change in the statutes since this decision was handed down, and the Commission could not at this time, or at any other time, without thirty days' notice change in any respect the orders which it made, or set them aside. If the Commission itself could not do so, clearly counsel cannot.

Under the statutes and this decision, the Commission could not attempt any application of its finding of the city gate rate to local rates without thirty days' notice. It could not in the proceeding now under consideration give notice of a hearing as to local rates for any one of the 135 cities involved, for it has repeatedly said this is not a rate case (as its order calling the investigation shows); has repeatedly refused to receive or consider evidence as to local rates, and has taken the definite posi-

tion in this Court that local rates were not involved (a position entirely inconsistent with the fact that a rate order, Exhibit "M," was actually issued). Also the voluminous record so far made is as to all companies, not as to any one, and it would be impossible for any one distributing company to present to any court the matter of its local rates as distinguished from rates for the whole 135 properties. This is exactly the position the Commission and its counsel at the time took as is shown by the following quotation from the proceedings set out at page 166 of our original brief:

> "Mr. Hatcher: We are not taking the position here, are we, or are you, Judge, that the over-all picture shows a decrease in rates? There may need to be reductions in some places, they would have to be treated separately, and the way this evidence has gone in, it has gone in collectively."

If the Commission cannot reopen this case and treat it as a case involving local rates for one company, all it could possibly do would be to issue another order under a separate docket number and start all over again, in which event nothing done in the past would be competent, relevant or material.

In this connection it should be borne in mind that the counsel who appeared for appellant in this Court are not state officers or even regular employees of the state. The Kansas Commission has its own attorneys, and the Attorney General has his own assistants. None of these attorneys or assistants appeared in this case, but on the contrary the Commission and the State are represented solely by special attorneys hired for the purposes of this case and none other. In their brief which was presumably prepared under the direction and subject to the approval

of the Commission, there is no indication of any such claim or contention as was made on oral argument, and we submit that counsel were without power or authority to speak for the Commission or bind it in any respect as to the nature of the proceeding which it conducted, or its future intentions with respect to such proceeding.

The section of the statute under which the costs of $66,936.08 were taxed against appellees, we have heretofore quoted. This statute shows that the taxing of costs is the last thing to be done in an investigation, and can only be done at the conclusion of an investigation. The statute contemplates that upon such order being made, the parties subject to the payment of the tax have the right to immediaely go into court and have the reasonableness and legality of the Commission's order determined. If the order is by the court held to be illegal or unreasonable, the order taxing costs falls. If this proceeding, as contended by counsel on oral argument, is merely a step in the process of rate making, then there is no protection whatever given appellees as to the payment of these costs.

In the foregoing discussion we have undertaken to consider general principles of law without regard to the Kansas statute except as that statute limits all power on the part of the Commission to conduct such an investigation to a proceeding

> "—in ascertaining the reasonableness of a rate or charge to be made by a public utility."

We have, however, called the Court's attention to the fact that the Kansas Commission is a creature of the statutes and has no power other than that expressly granted. This statute which we have set out at page 2 of

our original brief not only limits the power of the Commission to an investigation concerning rates, but expressly limits the nature of the showing which the Commission can require as to the cost of services and commodities furnished by affiliated companies. This part of the statute is as follows:

> "Such showing shall consist of an itemized statement furnished by the utility setting out in detail the various items, cost for services rendered and material or commodity furnished by the holding or affiliated company."

Instead of following this mandate of the statute, the Commission undertook to order the several appellees herein to make a valuation of the entire property of the Cities Service Gas Company, undertook to do so itself, and undertook to proceed in exactly the same manner as if it were determining the price to be charged by the Cities Service Gas Company for the commodity sold by it in inter-state commerce. We submit that under the foregoing statute the entire proceeding of the Commission was unauthorized and void.

If the proceeding before the Kansas Commission is to be considered as a completed rate case with a final order establishing rates for domestic consumers (as it must be or the final order, Exhibit "M," would not have been issued), then the court below had jurisdiction as otherwise rates would be now in effect not even producing operating expenses, the appellees would be foreclosed and estopped to question the reasonableness or legality of the thirty cent city gate rate in all future proceedings and the costs of $66,936.08 would be collected. It is only the injunction below which prevented the happening of all these things, or now prevents them. A removal of

the injunction by dismissal of the case below would leave the plaintiffs where they were originally, with confiscatory rates, the cost burden of $66,936.08, and a lack of opportunity in the future to question the reasonableness or legality of the city gate rate found by the Commission. If the case below should be dismissed, there is nothing whatever to prevent the Commission from again changing its mind and attempting the enforcement of its orders now enjoined. The Commission said in the beginning and all through the lengthy course of the hearings before it that the proceeding was not a rate case, then made it one; said the plaintiffs would be foreclosed to question the city gate rate found by the Commission, then said in oral argument here they would not. There is no protection in self-serving declarations by the Commission as to what it intends to do. There is no record of what has been said here on oral argument, nor any reason to believe the Commission approves or, in the absence of judicial restraint, will recognize the statements here made. The court should hold the proceeding before the Commission to be a completed rate case, and that the court below had jurisdiction.

If the proceeding instittued by the Commission was not a rate case, then the Commission had no authority to act under the Kansas statutes or the decisions of this court; had no authority to order 135 separate properties before it and then refuse them a hearing as to local rates; declare them foreclosed to question the Commission's findings; tax them with costs amounting to $66,936.08; cause them to incur an expense of $250,000; go out of the state and the limits of its jurisdiction to value property used in interstate commerce and make audits of the books of an interstate company; undertake to regulate interstate commerce by eliminating operating expense items, and

end it all with a rate order fixing local rates. If not a rate case, then it is not a step in such a case for there is no rate case in which it can be a step.

In any view which may be taken of the proceedings had, an order in two parts was issued, finding a city gate rate and putting it into effect by establishing local rates based thereon. This two-part order and each part of it were alleged in the bills of complaint filed in the court below to be invalid and unconstitutional for many federal reasons, and the court found them so to be and decreed a permanent injunction. The court below treated the two orders as in effect one, and in the same manner as if the order issued July 20, 1932, was before it for consideration, instead of that same order divided into two parts. As stated in the original brief, when the part of the order applying the findings of the Commission to local rates was admitted to be invalid and was found by the court to be confiscatory, each and every part of the two orders should have been permanently enjoined. *The appellant did not appeal from the decree of the court below permanently enjoining that part of the orders fixing local rates* (*Exhibit "M"*); the injunction as to that order is not before this court and in our view of the case this court has no authority at this time to set it aside or order a dismissal of the case in the court below. If set aside, such action by this court would in effect be and would be construed as an approval of all that the Kansas Commission has done, and would be construed by the Commissions of Missouri, Oklahoma and Texas as giving them and each of them authority to do the same thing, cause the same expense, tax the same costs, make the same valuations of property used in interstate commerce, the same audits of interstate business, substitute their judgment for the business

judgment of the officers and directors of an interstate company, regulate such interstate business by the elimination of items of operating expense, and generally burden such interstate commerce in such manner as to ruin it utterly; and all this under the claimed authority of the decision of this court in the case of Smith against Illinois Bell Telephone Co., and the decision of this court in the case of *Western Distributing Company* v. *Public Service Commission.* Surely, plaintiffs below were entitled to relief against this outrage, the court below had jurisdiction to grant the relief prayed for, and this court should affirm its decree or dismiss the appeal.

In this brief we have not attempted to cover the discussion as to jurisdiction set out in pages 1 to 51 of our original brief, all of which we consider material in the consideration of the questions here presented.

It should also be borne in mind that so far as the court below was concerned, jurisdiction did not depend upon a federal question alone but as to three of the plaintiffs, the Western Distributing Co., Union Public Service Co., and Cities Service Gas Co., attached by reason of diverse citizenship of the parties.

This court should judge the Commission by what it did and not by what it said or now says, and should hold that the proceeding before it was a rate case completed by a final order fixing local rates, Exhibit "M," admitted to be invalid and found by the court below to be void for the reason that it established confiscatory rates, and because plaintiffs were denied due process of law by reason of the refusal of the Commission to hear any evidence upon which valid local rates could be established, and this appeal should now be dismissed because appellant did not appeal from the decree permanently enjoining it and there is nothing before this

court for determination, or the decree below should be affirmed.

If the court should, however, hold the proceeding to be a mere step in an incomplete rate proceeding, it should hold such proceeding unauthorized by the Kansas statutes or the decisions of this court, and a proceeding the purpose of which was to determine one item of operating expense, the determination of which would be conclusive in 30 days unless appealed from, and then proceed to the determination of some other item, the determination of which would likewise become conclusive in 30 days, eventually leaving nothing but the final determination of one element open to review, and should affirm the decree of the court below, for the reason that such practice is open to every constitutional objection and should be condemned.

Throughout the entire course of this proceeding we have never known or been able to find out what it was all about, what the Commission intended to do, or where it would end. It has changed its position constantly and we have been compelled to meet the changes as best we could. We contend, however, that the best evidence of what the Commission intended to do is what it actually did, and that is, establish local rates for 135 properties in one proceeding in which it refused repeatedly to hear any evidence on which to base local rates. It admits the order as to local rates is void, which the court below found, and attempts to save itself by saying that it did not intend to do what it did and that the order fixing local rates should be forgotten and forgiven and it should be permitted to start over again. Where it will start, where it will go, or where end, it does not even suggest.

The only answer is, that the whole proceeding was unauthorized, violated every constitution principle of due

process of law and that no lawful or valid orders did or could or in the future can result therefrom. It is not a step, but the end of a misconceived, unfair, unreasonable, unauthorized and unconstitutional course of conduct which should be emphatically disapproved.

We desire to call the Court's attention to the fact that this brief is on behalf of the appellees other than the Cities Service Gas Company and that we have not undertaken to discuss the issues presented on oral argument as applying to it. The Cities Service Gas Company filed a separate bill of complaint in the court below (R. 184) which presented an entirely different issue from that presented by the distributing companies. The Cities Service Gas Company was not a party to the proceeding before the Commission and the orders complained of were not directed to it. Its cause of action was based on the fact that the Commission had by reason of its illegal action issued orders to its customers, the effect of which was to destroy its business. The decree entered by the court below was in favor of the Cities Service Gas Company as well as all the other appellees herein, and this court should in considering the issues now presented also consider the allegations of the bill of complaint of the Cities Service Gas Company, its brief, the assignment of errors filed by the appellant, and the decree of the court below as the same applies to the allegations of the bill of the Cities Service Gas Company.

Respectfully submitted,

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ROBERT STONE,
Topeka, Kansas,
Counsel for Appellees other than the Cities Service Gas Company.

APPENDIX.

Section 66-151 of the Revised Statutes of Kansas, 1923, is as follows:

> "Certified copies and conclusiveness of rates, regulations and orders. Upon application of any person, the commission shall furnish, free, certified copies of any classification, rates, rules, regulations, or orders; and such certified copies, or printed copies published by authority of the public utilities commission, shall be admissible in evidence in any suit, and sufficient to establish the fact that in any charge, rate, rule, order or classification therein contained, and which may be in issue in the trial, is the official act of the public utilities commission; and such determinations and orders of the commission shall be *prima facie* evidence, in any action in which they are offered, of the reasonableness and justness of the classifications, rates and charges involved therein and of all other matters therein found and determined; and after the lapse of thirty days from the time such determinations and orders shall be made, no suit then pending to set the same aside, and they remaining in full force and effect, such determinations and orders shall be held to be conclusive as to the matters involved therein. A substantial compliance with the requirements of this act shall be sufficient to give effect to all determinations and orders made and established by the commission. (L. 1905, ch. 340, Sec. 11; March 21.)"

We invite the Court's attention to the consideration of this statute in connection with our argument that appellees were compelled to go into court at the time these suits were filed, or would thereafter be forever foreclosed from so doing, and that no statements made to this Court by attorneys for appellant can change the force and effect of the above statute.

ROBERT D. GARVER,
Kansas City, Missouri,
ROBERT STONE,
Topeka, Kansas,
Attorneys for Appellees other than the Cities Service Gas Company.

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The Supreme Court of the United States

OCTOBER TERM, 1933.

No. 114.

THE STATE CORPORATION COMMISSION FOR THE STATE OF KANSAS, HOMER HOCH, JESSE W. GREENLEAF, ET AL.,
APPELLANTS,

vs.

THE WICHITA GAS COMPANY, HUTCHINSON GAS COMPANY, NEWTON GAS COMPANY, and CITIES SERVICE GAS COMPANY, ET AL.,
APPELLEES.

SUPPLEMENTAL BRIEF FOR APPELLEE, CITIES SERVICE GAS COMPANY, ON QUESTIONS ARISING ON ORAL ARGUMENT.

The tergiversation of appellants is obfuscating. Their chameleonic dexterity makes it difficult to trace their tortuous path. Like the parricide pleading for protection and mercy from the sentencing court because he is an orphan, they seek to capitalize their own perpetrated wrongs and gain a positive advantage by their own confessions. The penitent becomes greater than the inno-

cent. Absolution not only for wrongs confessed, but immunity from expiation of concomitant transgressions is claimed because of the confessions.

Appellants claim that after confession of wrong, without reparation by rescission or any step to remove the detriment to the business of the pipeline company, the case became moot and should have been dismissed.

The distributing company appellees have claimed that as to them the appeal became moot by reason of changed conditions, as the N. R. A., and other things recited in their brief.

Cities Service Gas Company has not claimed or conceded that the case below was moot in any phase or that the appeal is so; but if the court below acted on an inane, innocuous thing, without binding force for or against anyone, as contended by appellants in this court, in contradiction of their contentions in the trial court, as they confessed in answer to pungent questions propounded by them by members of this court, then such action by the trial court in enjoining the enforcement of it was certainly harmless, and if it was error, surely it was harmless error. We know of no court that reverses or modifies the decree of a trial court because of technical error that is harmless, a purely academic thing.

Appellants deliberately admitted in oral argument in this court that the findings as to fair price of gas and the orders to distributing company appellees to refrain from entering upon their books or considering in their rates charged more than thirty cents per m. c. f. were not res

judicata and had no inherent binding force upon anyone. They claimed that it was only one step on an uncharted course, which they now say led to seperate rate hearings; that they only intended to use the information gathered as evidence in such hearings. This is novel and ingenious. The testimony might be of value to use in such hearings, but of what use would the finding be as evidence if the proceeding was not completed and if it bound no one and of what use would the order to deal with nothing above thirty cents for gas either as to book entries or charges to customers be as evidence. It is an anomaly for the initiator, the prosecutor, in fact, who also happens to be the judge or trier and decider in this proceeding, to pause in media res just long enough to emit a finding and order concluding the precise point to be determined, in order that such finding and order might be used as evidence in deciding the question decided by the finding used to assist in deciding the question decided by the finding. The old masters dubbed such process circulus in probando.

We believe the moment appellants conceded that nothing done by the Commission had any binding force for or against anyone, their appeal became moot and subject to instant dismissal, not only because by such admission they admitted that the trial court had done a harmless thing—and no one is aggrieved by a harmless error—but also because the decree of the court did not purport to prevent or obstruct their using the evidence and testimony gathered in any manner they saw fit, either

in another "step" of the proceeding which appeared to be decided but which appellants now claim was not decided at all but was merely a preliminary flourish or fanfare to call all persons to the real hearing unsuspected, unannounced and uncharted, or in any other manner. This court is well justified in dismissing this appeal because the decree of the court below does not prevent appellants from doing all that they now deliberately profess, and have orally told this court, they wish or intend to do.

While we feel, from the evidence, that if this suit had not been brought and any of our customers (the distributing companies) had entered on their books more than thirty cents, had recorded therein a bill for forty cents, had considered more than thirty cents in their charges to their customers, that such customer would have felt the pains and penalties provided for disobedience of orders, yet since appellants now disavow such intent, the decree challenged by their appeal does not aggrieve the distributing companies.

Appellants persist in ignoring the suit and decree of Cities Service Gas Company. It was consolidated with the other suit merely for convenience of trial. We lost no rights by such consolidation. Our decree is just as binding as that in favor of any other party to this consolidated case. While we have not moved to dismiss because no citation was served on us and no chance given to us to participate in the selection of the portion of the record to be certified up or the portion to be printed, yet

we do protest against any attempt to tie our fortunes to those of other appellees or to bind us by any statement not made by us or adopted by us.

While we have not claimed that either the case or the appeal is moot we do contend that the case can be decided by this court without a decision of the questions as to the value of our properties, our proper expenses or what is a reasonable profit for us to ask for our product. Indeed we do not think a decision of those things is necessary in the least to support the decree of the trial court.

A skeleton outline of events will be persuasive as to what the Commission was intending and attempting to do and what they were doing to us when we sued.

In quick succession came the decision of Smith vs. Illinois Bell Tele. Co., 282 U. S. 133, the enactment of Chap. 239, Session Laws of 1931 of Kansas and the calling of this hearing by appellants to determine the reasonableness of our contracts with affiliated customers. If appellants then thought any other law of Kansas authorized them to hold any hearing upon the question of what a utility should pay for what it used, as for instance typewriter ribbons, lead pencils, stationery or any other necessary supplies, then why did they carefully segregate only our customers who were affiliates? No other law of Kansas than said Chapter 239 differentiated between transactions between affiliates and those with strangers. The highest court in the then circuit containing Kansas had solemnly decided that a public service commission had no business to interfere with con-

tracts for supplies bought by the utility from others, but that its only proper function was to deal with and regulate its transactions with those it served, its customers, the public.

Henry Oil Co. vs. The City of Nowata, (8th Circuit) 269 Fed. 742.

The appellant was affected with knowledge of this decision, and it is fair to presume that their counsel actually knew it. This makes it very persuasive, conclusive in our own minds, that the Commission intended to proceed under Chapter 239, the new law. If not, why not?

The Commission grounded its jurisdiction upon the affiliated relation. (R. 73)

The notice of the hearing said nothing concerning a rate hearing. It was, "concerning the reasonableness of contracts and charges made by holding companies to subsidiary companies of the Cities Service Company." (R. pp. 25-27) The body of the order made no mention of rates or a rate hearing. The title and body indisputably show that the Commission set out to do just exactly what it did: find the contract of this appellee for sale of gas unreasonable, lop off the alleged excess, direct our customers to discontinue recording or considering such excess and ordering them to pass on the amount saved, by the reduction in our price, to the consumers. The notice, the proceeding, the order (first an integral one and on rehearing a cloven or bifurcated one, the same as the first, mutatis mutandis, except there are two title assemblies and two sheets of paper) all show

without dissimulation or equivocation that there was to be no rate hearing; that the contract price of gas bought was to be lopped off by 25% and that same amount was to be subtracted from aggregate sales price to consumers unless cause could be shown against such result at a date too late to appeal from the order as to price to be paid to us and to be charged to the consumer.

Our business was a single one and was interstate. If the decision of this court in the Kansas Natural cases cited in our brief were no longer res judicata because of lapse of time and possible change of condition, still the answers of counsel for appellants, on the argument, to the Chief Justice of this court as to whether our business was interstate and whether the Commission had jurisdiction over us, have irrevocably settled those questions in this court for this case. They squarely and explicitly admitted our interstate status and that they had no power to regulate our business.

We alleged, and the record shows, diversity of citizenship, that the controversy involved more than $3,000, in our suit. We alleged illegal impairment of our contracts, unlawful interference with interstate commerce, deprivation of property without due process. For the District Court to have jurisdiction diversity of citizenship and the requisite magnitude of controversy were all that were necessary. To obtain the relief asked irreparable injury and inadequacy of legal remedy should, and did, appear. Because unconstitutionality of the order sought to be enjoined was alleged a three judge court was called, composed of two circuit judges and one district judge.

On oral argument counsel for appellants claimed that the Trial Court had no jurisdiction when the decree was entered. They now in supplemental brief admit they had jurisdiction and that instead of claiming a dismissal to be proper when they confessed their illegal acts, they now claim that the court simply went too far and that this court should modify the decree below. They do not now nor have they in their original brief nor did they in the oral argument show wherein the decree harmed them nor how they are aggrieved.

If the acts of appellants were unlawful and did us irreparable injury and we had no adequate remedy at law, then regardless of constitutional questions, or the reasonableness of our contracts we were entitled to the decree that was rendered. Since appellants admit jurisdiction of the court at the inception of the trial we spend no time on that. Jurisdiction once granted in a court of equity it will decide all questions necessary to a complete determination of the action. If the case can be decided on other than constitutional grounds the court will do it.

If, however, as appellants contend no constitutional question is involved in the portion of the decree appealed from then this appeal should be dismissed because it should have been taken to the Circuit Court of Appeals. In re: Buder, 271 U. S. 461.

Appellants in their supplemental brief do not in reality challenge the power of the court to decide, but really say that the court improperly exercised that power in that it decided wrongly instead of rightly; in that it en-

joined the enforcement of an order that the Commission did not intend to enforce against anyone; in that it prevented them from doing what they did not wish to do. They asked this court to prevent the trial court from preventing them from doing a thing they do not wish nor intend to do. If our analysis is correct we feel that this court will not feel called upon to settle such an academic question.

But we contend the decree was right and was necessary. Ab initio the proceeding was illegal. The Commission being a creature of statute, unknown to the common law had no powers except those the statutes gave it. They gave none to impair the obligation of a contract by a direct assault upon it. That the contract was one at the will of the parties makes no difference. As was said by this court in Truax vs. Raich, 239 U. S. 38, 60 L. Ed. 134, "The fact that the employment is at the will of the parties, respectively, does not make it at the will of others."

That fact that a public utility cannot disable itself from obeying valid orders of a commission by making contracts surely does not render the other party to a contract subject to unlawful assaults upon the contract simply because it has contracted with a public utility. Had the Smith vs. Illinois Bell Tele. Co. case, 282 U. S. 133, under which doubtless said Chapter 239 was attempted to be framed, been followed or had the statute been followed, then there would likely have been no complaint on our part for probably any impairment of our

contracts, interference with our interstate commerce or taking of our property, would have been slight, remote, indirect and by due process; the corporate autonomy and power of management of our customers would not be destroyed and they would still be able, as other business corporations, to contract with us and buy our products if by the exercise of good business judgment they could so mould their affairs that they could meet the rate to the customer properly prescribed in a rate hearing and pay us a price which we would be willing to accept. If commissions can single out and directly strike at contracts concerning large elements of cost of operations of a public utility they can have hearings upon and directly strike down every contract or purchase a utility can make and pursuing the course to the end they will have directly prescribed the kind of contract or purchase a utility may make in each and every detail, in all of the minutiae of daily transactions. Public utilities will then have become mere puppets, marionettes, simulácra, and the limitations upon commissions in usurping control of the affairs of utilities so forcefully outlined by this court in the cases cited by us on pages 21 and 22 of our brief will have been circumvented and rendered nugatory. "'Tis Greece but living Greece no more" would become an appropriate epitaph for the dead hands of utilities that henceforth guide nothing. Then public ownership should supplant private ownership so that financial risk and responsibility may become the burdens of those who control.

Since it is agreed that the proceedings of the Commis-

sion, if carried to consummation, would take from us $1,926,145.07 annually (R. 373) then if this deprivation of property was unlawful, surely this court should uphold our decree upon such agreed fact alone. Resort to the merits involving the exact figure that would constitute confiscation would seem superfluous.

Injunction is prevention, not redress. It is idle to say our action is premature, to wait until harm is done. Who will repay us for loss? A multiplicity of suits might bring judgments, but if consumers refuse to pay to our customers bills based on items the Commission has ordered our customers not to "consider" in their charges to their consumers, bankruptcy for someone looms large, and since it is agreed by appellants that our business cannot continue without the patronage of our proscribed customers (R. 213), their bankruptcy would be the necessary forerunner of ours.

In Pierce vs. Society of the Sisters of the Holy Name of Jesus and Mary and the consolidated case of Pierce Military Academy, 268 U. S. 510, 69 L. Ed. 1070, where action was brought to enjoin enforcement of a statute that did not "become effective for two or three years" this court held that the action was not premature if demoralization or impairment of business was probable, saying that "These are threatened with destruction through the unwarranted compulsion which appellants are exercising over present and *prospective* patrons of their schools."

In Pennsylvania and Ohio vs. West Virginia, 262 U. S. 553, 67 L. Ed. 117, this court held that an injunction,

against enforcement of a law, brought eight days after its passage and before any steps had been taken to enforce it was not premature the court saying: "One does not have to await the consummation of threatened injury to obtain preventive relief. If the injury is certainly impending that is enough."

Can there be any reasonable doubt that but for the institution of this suit, especially in the light of the confession of counsel for appellants on oral argument that they contended before the lower court that all findings and orders of the Commission would be res judicata upon our customers, that if our customers had entered our bills on their books as rendered and had "considered" such amounts in billing their customers, that they would have been proceeded against for violation of the orders of the Commission. Officers are presumed to do their duty and counsel *then* conceived it their duty to enforce those orders. True, the legality and binding force of laws or orders cannot be changed by talking about them, but the actual operations that would follow promulgation of orders would demoralize business even if the operator should afterward—long afterward, as counsel in this case have done, should conclude the operation of the order was harmless as it bound no one.

It is trite law that a litigant cannot seek reversal of a decree on a ground not presented to the trial court. This is but fairness to a busy court of first instance, where decision and action must be prompt and sometimes immediate. A fortiori no party should be allowed to procure a reversal upon a given point, where by reason of

his attitude before the trial court he led that court to believe a certain condition, course of conduct or result would ensue from his own act, and the court enjoined the act because of the confessed result, by a tergiversation before the reviewing court whereby he professes he was mistaken before the trial court. If there be error it is invited error. The equitable principle of estoppel applied should prevent the party from complaining of the result he had helped to cause. His attitude could not change the law, but he should be estopped from challenging the action of the lower court in enjoining a thing he now claimed harmed no one, which to the trial court he represented as potent of and pregnant with untoward effect. It is the threatened result that the trial court enjoins, not rightful legal result that would ensue. It is no ground for reversal for counsel to now state in open court that their position in the lower court was untenable and that the enjoined order was not, as was then claimed, absolutely binding.

Even if the enjoined order was void, we are entitled to be protected against its unlawful enforcement where plaintiff cannot by refusal to obey the order save itself from harm as was alleged in our petition. (R. 221)

For reason that the decree of the trial court prevented a wrong to us consisting largely of the manner of infliction of same and the further reason that appellants are estopped of complaining of the decree and are not really aggrieved thereby we respectfully contend that this court

is warranted in affirming the decree in favor of Cities Service Gas Company and that such affirmance should be had regardless of all other questions in the case.

Respectfully submitted,

JAS. W. FINLEY,
R. E. CULLISON,
Counsel for Appellee,
Cities Service Gas Company.

SUPREME COURT OF THE UNITED STATES.

No. 114.—October Term, 1933.

The State Corporation Commission for the State of Kansas, Homer Hoch, Jesse W. Greenleaf, et al., Appellants, *vs.* The Wichita Gas Company, The Hutchinson Gas Company, The Newton Gas Company, et al.	Appeal from the District Court of the United States for the District of Kansas.

[January 8, 1934.]

Mr. Justice Butler delivered the opinion of the Court.

Ten suits were consolidated for trial.[1] The appellee in each of the first nine is a local public service corporation, for convenience called a distributing company, engaged in the business of furnishing natural gas to consumers, domestic and industrial, in Kansas, and together they operate in 128 cities and towns. The other appellee, Cities Service Gas Company, is a pipe line company, engaged in transporting gas from Texas and Oklahoma fields into Kansas and other States. The stock of each of the distributing companies is owned by the Gas Service Company, and its stock is owned by the Cities Service Company; the common stock of the Cities Service Gas Company is owned by the Empire Gas and Fuel Company, the voting stock of which is owned by the Cities Service Company. Henry L. Doherty, doing business as Henry L. Doherty & Company, owns 35 per cent. of the voting stock of the Cities Service Company. The policies of the distributing companies and the pipe line company are subject to control by the Cities Service Company and Doherty controls its policies. These

[1]The appellees are: The Wichita Gas Company, The Hutchinson Gas Company, The Newton Gas Company, The Pittsburg Gas Company, The Capital Gas & Electric Company, The Wyandotte County Gas Company, The Girard Gas Company, Union Public Service Company, The Western Distributing Company, Cities Service Gas Company.

corporations and he constitute "affiliated interests" as defined by a Kansas statute effective March 9, 1931,[2] the substance of which is later to be stated.

The Kansas statutes empower its public service commission to regulate the service and to fix rates to be charged by public utilities including the distributing companies.[3] They prescribe heavy penalties for failure to comply with commission-made orders.[4] But the sale, transportation and delivery of natural gas by the pipe line company to the distributing companies constitutes interstate commerce and therefore the State is without power to prescribe rates or prices to be charged therefor. *Missouri* v. *Kansas Gas Co.*, 265 U. S. 298, 305, *et seq.* *Peoples Gas Co.* v. *Pub. Ser. Comm.*, 270 U. S. 550, 554. *Pub. Util. Comm.* v. *Attleboro Co.*, 273 U. S. 83, 90. *Smith* v. *Illinois Bell Tel. Co.*, 282 U. S. 133, 148.

The Act of March 9, 1931, § 1, gives the commission jurisdiction over holders of the voting stock of public utility companies to the extent necessary to require disclosure of the identity of the owners of substantial interests therein, and provides that the commission shall have access to the accounts and records of affiliated interests, relating to transactions between them and public utility companies. Section 2 declares that no management or similar contract with any affiliated interest shall be effective unless first filed with the commission and authorizes the commission to disapprove any such contract found not to be in the public interest. Section 3 provides: "In ascertaining the reasonableness of a rate or charge to be made by a public utility, no charge for services rendered by a holding or affiliated company, or charge for material or commodity furnished or purchased from a holding or affiliated company shall be given consideration in determining a reasonable rate or charge unless there be a showing made by the utility affected by the rate or charge as to the actual cost to the holding or affiliated company furnishing such service and material or commodity. Such showing shall consist of an itemized statement furnished by the utility setting out in detail the various items, cost for services rendered and material or commodity furnished by the holding or affiliated company".

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[2]Kansas Laws, 1931, c. 239; Kan. R. S., §§ 74-602a, b, c.

[3]Kan. R. S., §§ 66-107, 66-110, 66-111, 66-113.

[4]Kan. R. S., § 66-138.

July 2, 1931, the commission, exerting powers granted by the Act, ordered an investigation of the charges made by holding companies for services rendered and commodities furnished to the distributing companies. It directed them to give the commission such information as they might see fit and as the commission might require; it ordered them to show cause why charges made by any holding company, if found unreasonable, should not be disallowed as operating expenses. The order was not directed to Henry L. Doherty & Company, the pipe line company or any holding company, and none of them appeared or became a party to the proceeding before the commission.

And, pursuant to the order, there were held extended hearings at which there was submitted much evidence as to the value of the pipe line company's properties located in five States, its operating expenses, including depreciation and taxes, and its gross revenues and income available for return. In short, the facts adduced were such as appropriately might be considered by a commission for the ascertainment of reasonable rates to be charged by the pipe line company, or by a court in determining whether established rates are confiscatory. Each distributing company tendered proof of the value of its own property used to furnish gas to its customers together with other facts essential to the determination of the reasonableness of the rates then being, and later to be, charged its customers. But the commission, not then being engaged in the investigation of the reasonableness of such rates, refused to hear evidence other than that bearing upon the reasonableness, as operating expense items, of charges made by affiliated interests for services rendered the distributing companies and especially of prices exacted by the pipe line company for gas delivered in interstate commerce at the gates or borders of the various cities and communities served by the distributing companies.

The commission held payment of 1¾ per cent. of their gross earnings to Henry L. Doherty & Company unwarranted and the prices paid the pipe line company for gas unreasonable to the extent that they exceeded 29.5 cents per thousand cubic feet.[5]

[5]Throughout the record the city gate rate is referred to as the "40-cent rate". That is the usual charge per thousand cubic feet of gas delivered by the pipe line company to the mains of the distributing companies. But as in some instances the city gate rate was lower, the average was 39.5 cents.

P: U. R. 1933A, pp. 113-202. It granted the companies' application for rehearing, and August 31, 1932, put aside the order filed with its report and in its place promulgated two orders:

The first directed the distributing companies to cease setting up as an expense item payment of the 1¾ per cent. charge and payment to the pipe line company for gas in excess of 30 cents per thousand cubic feet and to give no consideration to the payments so disapproved in fixing rates to domestic consumers. And it directed that, on October 17, 1932, the distributing companies show cause why the preseribed reduction should not be passed on to the consumers.[6]

The second order directed that, effective September 1, 1932 and pending hearing and an order prescribing rates, "All distributing companies paying a gate rate in excess of 30 cents per M. C. F. shall deduct the difference between what the distributing company is now paying at the city gate and 30 cents per M. C. F. and pass on this difference to the consumer."

Apprehending that, as counsel for the commission asserted at the hearing, these orders would become final and absolutely binding unless within 30 days, §§ 66-113, 66-118, action were commenced to have them set aside, appellees brought these suits September 19, 1932. Each sued the commission, its members and the attorney general, invoking jurisdiction on the ground that its suit is one arising under the Federal Constitution. The complaint, upon the basis of fact set forth, asserts that the orders are repugnant to the commerce clause and the contract clause of the Constitution and to the due process and equal protection clauses

[6]The text is as follows:

"1. That on and after the 1st day of September, 1932, the distributing companies, respondents above named, shall cease to set up on their books as an expense item any payments made to Henry L. Doherty & Company under the contract above mentioned, because of the one and three-fourths per cent charge and also any payments made to Cities Service Gas Company for main line town border gas in excess of 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer.

"2. That on the 17th day of October, 1932, the distributing companies, respondents above named, appear before the Public Service Commission, at 10:00 o'clock A. M., and show cause to the Commission why the reduction in expenses as above set forth should not be passed on to the consumers with such other reductions as may be found reasonable."

of the Fourteenth Amendment and prays temporary and permanent injunction. The defendants moved to dismiss on the grounds that the bill fails to state a cause of action and that the court was without jurisdiction. A specially constituted court of three judges denied the motion to dismiss. The defendants answered, admitting that because repugnant to a state statutory provision the second order was unauthorized and is void. The court granted temporary injunction and tried the case upon the merits. It was submitted upon the evidence introduced before the commission, stipulations as to matters of fact and other evidence. The court made findings of fact and stated its conclusions of law. Equity Rule 70½. And it permanently enjoined the defendants from enforcing the orders in so far as they required the distributing companies to cease to set up on their books any payment to the pipe line company for gas in excess of 30 cents per thousand cubic feet, to give no consideration to such payments in fixing a rate for the domestic consumer and, commencing September 1, 1932, to charge rates reduced as directed by the second order.[7]

The first order does not purport to establish or prescribe prices to be paid by the distributing companies to the pipe line company or purport to establish any rate to be charged by appellees to their customers. It merely directs the distributing com-

[7]Paragraph (3) of the decree:

"That the defendants, the Public Service Commission of the State of Kansas, and the members thereof, and Roland Boynton, Attorney General of the State of Kansas, and each of them, their agents, servants, and employees, and all other persons acting under or through their authority, be and they are hereby permanently enjoined and restrained in the enforcement and execution of the provisions of two certain orders of said Public Service Commission dated August 31, 1932, insofar as the said orders require that the distributing companies, plaintiffs in the above named cases, should cease to set up on their books any payments made to Cities Service Gas Company for main line town border gas in excess of 30 cents per M. C. F., and should give no consideration to any such payments in fixing a rate for the domestic consumer; and, insofar as they and/or either of them require that effective September 1, 1932, and until a hearing is held and an order issued, the said distributing companies should charge rates to the consumers as follows:

"All distributing companies paying a gate rate in excess of 30 cents per M. C. F. should deduct the difference between what the distributing companies were then paying at the city gate and 30 cents per M. C. F., and should pass this difference on to the consumer."

panies not to include in their operating expense accounts more than 30 cents per thousand cubic feet for gas furnished by the pipe line company and not to consider any payments in excess of that price in fixing a rate for domestic consumers.

We need not decide whether these provisions are repugnant to the Constitution or whether they are otherwise invalid. The invalidity of such an order is not of itself ground for injunction. Unless necessary to protect rights against injuries otherwise irremediable, injunction should not be granted. *Terrace* v. *Thompson*, 263 U. S. 197, 214. Appellees in substance suggest that, unless now adjudged invalid and enjoined, the findings and directions of the commission in respect of their operating expenses and the fixing of rates will be binding upon them in later proceedings for the prescribing of rates to be charged by them for gas furnished to consumers and in suits involving the validity of such rates. But the commission's proceedings are to be regarded as having been taken to secure information later to be used for the ascertainment of reasonableness of rates. The order is therefore legislative in character. The commission's decisions upon the matters covered by it cannot be *res adjudicata* when challenged in a confiscation case or other suit involving their validity or the validity of any rate depending upon them. *Prentis* v. *Atlantic Coast Line*, 211 U. S. 210, 227. *Chicago, &c. Railway Co.* v. *Minnesota*, 134 U. S. 418, 452, *et seq.* But the decisions of state courts reviewing commission orders making rates are *res adjudicata* and can be so pleaded in suits subsequently brought in federal courts to enjoin their enforcement. *Det. & Mackinac Ry.* v. *Mich. R. R. Comm.*, 235 U. S. 402, 405. *Napa Valley Co.* v. *R. R. Comm.*, 251 U. S. 366, 373. The appellees were not obliged preliminarily to institute any action or proceeding in the Kansas court in order to obtain in a federal court relief from an order of the commission on the ground that it is repugnant to the Federal Constitution. *Bacon* v. *Rutland R. R. Co.*, 232 U. S. 134, 138. *Missouri* v. *Chi., Burl. & Quincy R. R.*, 241 U. S. 533, 542. *Ex parte Young*, 209 U. S. 123, 166. And upon the issue of confiscation *vel non* they are entitled to the independent judgment of the courts as to both law and facts. *Ohio Valley Co.* v. *Ben Avon Borough*, 253 U. S. 287, 289. *Bluefield Co.* v. *Pub. Serv. Comm.*, 262 U. S. 679, 689. *United Railways* v. *West*, 280 U. S. 234, 251.

It results, therefore, that appellees in their complaints failed to state facts sufficient to entitle them to a decree enjoining the appellants from enforcing the first order for, as insisted by appellants in oral argument in this court, the challenged provisions are merely preliminary steps in aid of investigations for the ascertainment of the reasonableness of appellees' rates, and they have no binding force in respect of payments to the pipe line company or rates to be charged consumers and cannot be *res adjudicata*. The decree in so far as it enjoins enforcement of the provisions of that order will be vacated.

The commission, its members and attorney general having in their answer and here admitted that the commission's second order is invalid, the decree in so far as it enjoins the enforcement of its provisions will be affirmed.

Decree modified and, as modified, affirmed.

A true copy.

Test:

Clerk, Supreme Court, U. S.